



# Village of Cornwall-On-Hudson

## Selected Financial Activities

### Report of Examination

Period Covered:

March 1, 2010 — April 30, 2011

2011M-155



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 2012

Dear Village Officials:

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

Following is a report of our audit of the Village of Cornwall-On-Hudson, entitled Selected Financial Activities. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

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

Respectfully submitted,

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



## State of New York Office of the State Comptroller

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# EXECUTIVE SUMMARY

The Village of Cornwall-On-Hudson (Village) is located in the Town of Cornwall in Orange County and serves approximately 3,100 residents. The Board of Trustees (Board) is the legislative body responsible for managing Village operations, including establishing appropriate internal controls over financial operations and maintaining sound financial condition. The Village's general, water, and sewer funds' total budgeted appropriations for 2010-11 and 2011-12 were approximately \$6.7 million and \$7.1 million.

### **Scope and Objectives**

The objectives of our audit were to review the financing and construction of the Village's Department of Public Works (DPW) building, the Village's financial operations, and the Village's information technology (IT) systems for the period March 1, 2010 through April 30, 2011. We extended our audit period to 2005 for the construction of the DPW building. We also included information dating back to 2000 and for the 2011-12 fiscal year to demonstrate trends for financial condition. Our audit addressed the following related questions:

- Was the Board's process for constructing the DPW building in the best interest of Village taxpayers?
- Did the Board sufficiently monitor the Village's financial operations and take appropriate actions to maintain the Village's financial stability?
- Did the Board ensure that the Village's IT systems were adequately secured and protected against unauthorized access and loss?

### **Audit Results**

The Board did not act in the best interest of Village taxpayers when it circumvented applicable State laws by using the Cornwall-on-Hudson Local Development Corporation (COHLDC) to construct the DPW building. We also identified significant deficiencies in the internal controls over financial operations and computerized data.

In 2005, the Board elected to have COHLDC construct a new DPW building to avoid compliance with State Laws. In addition, the Board issued a \$960,000 serial bond to finance construction and turned the proceeds over to COHLDC. However, the agreement between COHLDC and the contractor to construct the building was for only \$722,000. Although COHLDC eventually refunded a portion of

the excess financing to the Village, the final amount paid was \$929,000, which was \$207,000 more than the contract price. Furthermore, the Board did not have the site of the new building properly investigated and allowed the building to be constructed without the required permits. As a result, the taxpayers paid approximately \$1 million for a new DPW building that cannot be used because of building code violations.

The Board did not sufficiently monitor financial operations or take appropriate action to maintain financial stability. As a result, the Village will have an accumulated deficit of \$303,000 at the end of the 2010-11 fiscal year. The accumulated deficit and fiscal stress in prior years were the result of the Board's failure to adopt realistic budgets. The resulting cash flow problems required the use of revenue anticipation notes (RANs) to sustain operations. Since the 2000-01 fiscal year, the Board has issued RANs totaling \$990,000, incurring over \$245,000 in interest expense and still has \$585,000 to repay. The Board's 2011-12 budget also included unrealistic estimates that could result in a revenue shortfall of \$515,000, requiring a further need for short-term borrowing to sustain operations.

In addition, the Board did not adopt written policies and procedures for accounting operations. As a result, Village debt records were inadequate, 12 of the 46 late tax payments that we tested did not have correct penalties assessed and 15 of the 46 tax receipts tested were not deposited until over 20 days after receipt. Furthermore, inter-fund loans were created without Board approval, and wire transfers totaling \$5,800,000 were made without prior approval or a call back verification of the transfer. The lack of oversight increases the risk that errors or irregularities could occur and go undetected.

The Board also did not ensure that the information systems were adequately secured and protected. For example, the Board did not adopt guidance for assessing the IT system for security vulnerabilities, disaster recovery or acceptable use. In addition, remote access was granted to four users despite a lack of procedures to monitor their activities and there was no IT administrator until July 2010, which caused backups of Village data to not be run and tested. As a result, the Village has permanently lost valuable information and data.

### **Comments of Local Officials**

The results of our audit and recommendations have been discussed with Village officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, Village officials generally agreed with our recommendations and indicated that they planned to take corrective action. Appendix B includes our comments on issues raised in the Village's response letter.

# Introduction

## Background

The Village of Cornwall-On-Hudson (Village), which is located in the Town of Cornwall in Orange County, serves approximately 3,100 residents and encompasses approximately two square miles. The Board of Trustees (Board) is the legislative body responsible for managing Village operations, including establishing appropriate internal controls over financial operations and maintaining sound financial condition. Although the Board is primarily responsible for the effectiveness and proper functioning of the Village's internal controls, the Mayor, Clerk and Treasurer and department heads also share the responsibility for ensuring that internal controls are adequate and working properly.

The Mayor, who is a member of the Board, serves as the Village's Chief Executive Officer. During 2010-11, the Village had a full-time Treasurer, who was not reappointed for 2011-12. The current Mayor and Treasurer took office in April 2011. The Board appointed the Clerk to the Treasurer position, making her the Clerk and Treasurer for 2011-12. The Clerk and Treasurer is the Chief Fiscal Officer and is responsible for the receipt, disbursement and custody of Village moneys in addition to the maintenance of accounting records.

The Village's general, water, and sewer funds' total budgeted appropriations for 2010-11 and 2011-12 were approximately \$6.7 million and \$7.1 million, funded primarily with real property taxes, water and sewer charges and State aid. The Village provides various services to its residents, including law enforcement, fire protection, street maintenance, snow removal, street lighting, water, sewer and general government support.

In 2005, the Board elected to have the Cornwall-On-Hudson Local Development Corporation construct the new DPW building. COHLDC was formed in 1998.

Local Development Corporations (LDCs) are not-for-profit corporations often created for economic development or other public purposes, including stimulating economic growth, expanding job opportunities and reducing unemployment in the communities in which they exist. Their efforts may include attracting new industries to the community, retaining existing businesses and training individuals to improve job skills. LDCs have been given broad and independent powers under the governing statutes. These powers in some respects equal or exceed those of local governments. For example, LDCs may construct, acquire, rehabilitate and improve

industrial or manufacturing plants for use by others (e.g., private companies), or provide financial assistance to others to do so. LDCs do not have to comply with many of the statutory requirements that municipalities must follow. For instance, LDCs are not subject to bidding requirements and are not obligated to seek competition when procuring goods and services.

## **Objectives**

The objectives of our audit were to review the financing and construction of the Village's Department of Public Works (DPW) building, the Village's financial operations, and the Village's information technology (IT) systems. Our audit addressed the following related questions:

- Was the Board's process for constructing the DPW building in the best interest of Village taxpayers?
- Did the Board sufficiently monitor the Village's financial operations and take appropriate actions to maintain the Village's financial stability?
- Did the Board ensure that the Village's IT systems were adequately secured and protected against unauthorized access and loss?

## **Scope and Methodology**

We examined the construction of the DPW building, financial operations and information technology for the period March 1, 2010 to April 30, 2011. We extended our audit period to 2005 for the construction of the DPW building. We also included information dating back to 2000 and for the 2011-12 fiscal year to demonstrate trends for financial condition.

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 Local Officials and Corrective Action**

The results of our audit and recommendations have been discussed with Village officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, Village officials generally agreed with our recommendations and indicated that they planned to take corrective action. Appendix B includes our comments on issues raised in the Village's response letter.

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 Village to make this plan available for public review in the Clerk and Treasurer's office.

## Public Works Building

Capital projects are long-term projects which require relatively large sums of money to acquire, develop, improve, or maintain. The Board is responsible for oversight and management of the Village's capital projects. In 2005, the Board elected to construct a new DPW building. The Board was responsible for ensuring that the DPW building was constructed in compliance with State Laws, and for ensuring that the serial bond issued to finance construction was not for more than the amount necessary. The Board was also responsible for ensuring that the amount paid was reasonable, the building site was suitable, and the required permits were obtained for construction.

The Board elected to have the Cornwall-On-Hudson Local Development Corporation<sup>1</sup> (COHLDC) construct the new DPW building to avoid compliance with State Laws. The Board issued a \$960,000 serial bond to finance construction and paid \$929,000 for the building even though the agreement to construct the building was for only \$722,000. Furthermore, the site was not properly investigated and the required permits were not obtained. As a result, the taxpayers paid approximately \$1 million for a new DPW building that cannot be used.

### Proposed Building

In 2005, after receiving complaints from residents about the noise being generated from the existing DPW building, the Board decided that the Village would build a new DPW building on property the Village owned on Shore Road. The Board developed a plan which included the sale of the current building, with the proceeds of the sale used to help finance the construction of a new DPW building.

Acting upon the former Village Attorney's advice, the Board elected to have the DPW building constructed by COHLDC. COHLDC was formed in 1998.<sup>2</sup> According to a memo from the Village Attorney, the utilization of COHLDC "...would... accomplish the project without having to deal with the extra costs associated with the Wicks Law," The Wicks Law requires multiple prime contracts for public works projects for the construction of buildings when the entire cost

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<sup>1</sup> Local Development Corporations (LDCs) are not-for-profit corporations often created for economic development or other public purposes. LDCs have been given broad and independent powers. For example, LDCs may construct manufacturing plants for use by others (e.g., private companies), or provide financial assistance to others to do so. LDCs are not subject to bidding statutes and are not obligated to seek competition when procuring goods and services.

<sup>2</sup> COHLDC was initially formed for the "Riverfest" annual event, although the COHLDC is no longer involved.

of the work exceeds the dollar threshold set forth in the statute.<sup>3</sup> When the Wicks Law applies, municipalities must award separate prime contracts for three major components of the work: electrical, plumbing, and HVAC (heating, ventilation and air conditioning). A fourth contract often is awarded to a general contractor for the remainder of the project scope. Furthermore, General Municipal Law (GML) requires that political subdivisions competitively bid for public works contracts that exceed \$35,000.<sup>4</sup> Competitive bidding laws are intended to promote honest competition in order that local governments obtain quality goods and services at the best possible price and to guard against favoritism, extravagance, fraud, and corruption.

The Board advanced \$960,000 to COHLDC for the construction of the DPW building even though the contract agreement between the COHLDC and builder was only for \$722,000. Although the Village paid for the construction of the DPW building, it was built without adhering to GML bidding requirements. Furthermore, the Board did not exercise due diligence by having engineering/testing done on the proposed site and as a result is unable to use the building.

## **Bond Proceeds and Building Costs**

The original plan for the construction of the DPW building was to have the COHLDC construct the building and then lease it to the Village over a five year period with the Village taking ownership of the building after the lease expired. The Village initially planned to sell the old DPW building and use the proceeds of the sale to help finance the new construction. Instead, the Board issued serial bonds and turned over the bond proceeds of \$960,000 to the COHLDC in October 2005 for the construction of the building.

The Board advanced all the bond proceeds to the COHLDC rather than releasing the money as the work on the DPW building progressed or was completed. Furthermore, the Board did not require the COHLDC to obtain a performance bond or enter into a written contract with COHLDC to ensure that the building was constructed properly.

On August 1, 2005, the COHLDC signed an agreement with a contractor to construct the DPW building at a cost of \$722,000. In addition, the Village signed the old DPW building over to the COHLDC, which in turn sold the property for \$300,000. Therefore, the amount needed to finance the construction of the building was

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<sup>3</sup> At the time of the transactions at issue, the Wicks threshold was \$50,000. It has since been increased for local governments outside of NYC and Westchester, Nassau and Suffolk Counties to \$500,000.

<sup>4</sup> The bidding threshold at the time of the construction of the DPW building for public works contracts was \$20,000.

\$422,000. However, the Village advanced the COHLDC \$960,000 or \$538,000 more than was necessary to construct the building. The Village eventually received the \$300,000<sup>5</sup> from the sale of the old DPW building and a \$31,000 refund from COHLDC. However, the ultimate cost paid to COHLDC was still \$929,000 or \$207,000 more than the price per the contract between COHLDC and the contractor for the new DPW building.

Furthermore, because the COHLDC gave the Village \$300,000 from the sale of the old DPW building in May 2006, the Village could not use that money to reduce the amount of the serial bond issued in October 2005 to finance the new DPW building. We estimate the Village will incur approximately \$378,000 in interest over the life of the bond that could have been reduced if the Board had adhered to the original plan and used the proceeds from the sale of the original DPW building to help finance the new building.

The Village paid for the construction of the DPW building without being a party to the signed written contracts and without any assurance that the building would be properly constructed. Although the Village paid for the construction of the DPW building through the use of the COHLDC as the entity constructing the building, the DPW building was built without adhering to the Wicks law or bidding requirements under GML.

## Due Diligence

Due diligence refers to the care a reasonable person should take before entering into an agreement or a transaction with another party. The Board is responsible to act in the best interest of the Village taxpayers. The property on which the new DPW building was to be located on Shore Road is a former sewage treatment plant. Our review of correspondences and Board minutes showed that the Board was aware of problems with the use of this property as the construction site based on a 1973 investigative report.<sup>6</sup>

Therefore, the Board contracted with a second engineering firm in 2005 to review the previous soils investigation report. The second engineering firm concurred with the 1973 investigative report. The second engineering firm stated that the new DPW building is a “pole barn” structure which is built on a foundation slab. The 1973 engineering review stated that this type of construction was not suitable for the site. The May 2005 review concurred with the original soils investigation report and recommended a “pile foundation” type of construction be used on the site. A “pile foundation” type of construction is more costly than the “pole barn” type which

<sup>5</sup> Two payments in May 2006

<sup>6</sup> In 1973, a soils investigation report was done on the Shore Road property which found the land unsuitable for a proposed DPW garage at that time.

the engineer estimated at increasing the cost of the building by approximately \$230,000. Village officials represented that they had additional tests done on the site by another company in June 2005 and that the tests were inconclusive. However, there was no documentation showing payment to this company or the purported testing results.

The use of the Shore Road property for construction of the new DPW building was questionable based on the engineering reviews completed in 1973 and 2005. The Board disregarded the professional advice of the engineers and proceeded with plans to construct the new DPW building. The Board should have exercised due diligence by having further engineering/testing done on the site to determine if the site was suitable for construction of the new DPW building. Without proper planning and seeking professional advice on the use of questionable land, the Board may have expended funds not in the best interest of taxpayers.

## **Required Permits**

Upon completion of the DPW building in March 2006, the DPW began using the building, although a certificate of occupancy for the building was not issued.<sup>7</sup> Four years later, the Village Code Enforcement Officer refused to issue a certificate of occupancy for the DPW building apparently due to numerous concerns raised by the Department of State (DOS).

According to a letter from DOS to the Village regarding the DPW building, DOS has serious concerns with violations of the New York State Uniform Fire Prevention and Building Code (“Uniform Code”) and the State Energy Conservation Code.<sup>8</sup> DOS strongly recommended not occupying the building at that time because there was no assurance that the building structure was capable of safely sustaining gravity or lateral loading conditions to which it may be subject. Moreover, DOS advised the Village that the DPW building could not be occupied without a certification of occupancy and based on the documents provided by the Village a certificate of occupancy should not be issued until the Village can demonstrate that the building is in compliance with the Uniform Code.<sup>9</sup>

The DPW vacated the building in February 2010. Since then, DPW staff have been working out of a rented trailer. Vehicles and machinery are being stored outside at this time. The Village is incurring a cost of \$485 per month to rent the trailer. Because the COHLDC did

<sup>7</sup> Generally, a certificate of occupancy is issued when a building is in compliance with applicable building requirements.

<sup>8</sup> This information was in a May 17, 2010 letter to the Mayor from the Department of State.

<sup>9</sup> This information was in an email, dated February 18, 2010, from the Department of State.

not obtain the necessary permits when constructing the building, the Village took ownership of the building without acquiring a certificate of occupancy and the COHLDC did not ensure that the building was constructed to established standards, Village taxpayers have paid for a building which is not being utilized.

**Dissolution of the COHLDC** Village officials told us they believed that the COHLDC has been dissolved. A resolution dated December 31, 2007 to that effect was approved by the Board. However, because of inaccurate filings, the COHLDC was denied dissolution by DOS. Neither the Board nor the Village Attorney at that time followed up on the dissolution; therefore, although inactive, the COHLDC is still a legal entity.

The Board's use of the COHLDC to construct the DPW building was intended to avoid the constraints of the Wicks Laws and circumvent the bidding requirements municipalities must adhere to. Furthermore, the Board did not have the site of the new building properly investigated and allowed the building to be constructed without the required permits. As a result, the taxpayers paid approximately \$1 million for a new DPW building that cannot be used because of building code violations.

## **Recommendations**

1. When contemplating major construction projects, the Board should adhere to all legal statues concerning financing of capital projects and adhere to GML concerning bidding requirements.
2. The Board should exercise due diligence prior to engaging any individual/corporation to conduct business with the Village. The Board should enter into written contracts with such individuals/corporations to protect the taxpayers interests.
3. The Board should have an engineer review the apparent deficiencies of the DPW building and make a determination whether it is in the best interest of the taxpayers to have the building brought up to code.
4. The Board should take steps to have the COHLDC dissolved, if that is its intent.

## Financial Operations

The Board is responsible for ensuring that internal controls are in place to safeguard the Village's fiscal health and financial resources. A municipality is considered to have sound fiscal health when it can consistently generate sufficient recurring revenues to finance anticipated expenditures, and maintain sufficient cash flow to pay bills and other obligations when due. To accomplish this, the Board must adopt realistic budgets.<sup>10</sup> In addition, the Board is responsible for establishing controls for accounting operations to ensure interest is paid in the proper amount, tax receipts are accounted for, and inter-fund loans and wire transfers are properly approved.

Budget status reports indicate that the Village will have an accumulated deficit of \$303,000 at the end of the 2010-11 fiscal year caused by the Board's failure to adopt realistic budgets. This caused cash flow problems that required the use of revenue anticipation notes (RANs) to sustain operations. As a result, the Village incurred interest expense related to these borrowings. The Board's 2011-12 budget also included unrealistic estimates that could result in a revenue shortfall of \$515,000. Finally, inter-fund loans were created without Board approval and wire transfers totaling \$5,800,000 were made without prior approval or verification.

### Fund Balance

Fund balance<sup>11</sup> is the accumulated difference between revenues and expenditures that can be used to help provide cash flow and manage unexpected occurrences. Inadequate fund balance limits the ability of officials to manage emergencies and other unanticipated occurrences and can necessitate the need for short-term borrowing to sustain operations.

Although the Village's fiscal year ended on February 28, 2011, as of the end of our fieldwork on May 18, 2011, the Village's books and records had not been closed for the year-end. Therefore, fund balances for the 2010-11 fiscal year had not been finalized. Budget status reports as of the end of the fiscal year indicate the Village will have a deficit in one or more of its funds. Due to the poor recordkeeping associated with inter-fund loans,<sup>12</sup> Village Officials cannot determine which funds in particular will have a deficit until all inter-fund loans are recorded with adjusting year-end journal entries.

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<sup>10</sup> The Board must ensure that budgets are prepared and adopted based on the resources that can be used to fund operations. This requires the Board to balance the level of services desired and expected by Village residents with the ability and willingness of the residents to pay for such services.

<sup>11</sup> Unreserved, unappropriated fund balance

<sup>12</sup> See related comment entitled "Accountability, Inter-fund Loans"

As table 1 indicates, the water fund had deficit balances in 2008-09 and 2009-10. For 2010-11, based on preliminary numbers, the water fund may have a positive fund balance. However, when all fund balances are combined for 2010-11 the Village will have a total deficit of approximately \$303,000.

<b>Table 1: Fund Balances</b>			
	<b>FY 2008-09</b>	<b>FY 2009-10</b>	<b>FY 2010-11</b>
General Fund	\$14,520	\$125,412	(\$281,422)
Water Fund	(\$89,235)	(\$362,273)	\$310,800
Sewer Fund	\$73,099	\$243,265	(\$332,296)
<b>Total</b>	<b>(\$1,616)</b>	<b>\$6,404</b>	<b>(\$302,918)</b>

The deficit fund balances result from the Board’s failure to adopt realistic budgets. For example, every year from 2005-06 through 2010-11, the Board has budgeted revenue from a grant from the Federal Emergency Management Agency (FEMA) of \$220,000. Although the grant was approved for waterfront improvements, the Board did not appropriate any amounts for the work that had to be performed to receive the revenues, no work was ever performed to receive the revenues and the grant expires in the current fiscal year (2011-12).

For six fiscal years, the Board inflated revenues by including grant revenue that it knew it would not receive. This had a collective effect of creating a revenue shortfall of \$1,320,000 over the six-year period.<sup>13</sup> Consequently, the Board had to rely on RANs and inter-fund loans to sustain operations and, despite this reliance, could not avoid the deficit for 2010-11 discussed previously.

RANs – RANs are short-term debt securities issued on the premise that future revenues will be sufficient to meet repayment obligations. It is important that the Board pay off RANs with the anticipated revenues as soon as possible, and that the Board not reissue RANs on a perpetual basis in an effort to mask the Village’s under-lying budgetary and cash flow deficiencies.

The Village has consistently relied on short-term borrowing by issuing RANs to meet the Village’s cash needs. However, instead of paying off the RANs with the anticipated revenues, the Board issued new RANs each year to raise the money to pay off the previous year’s debt. The Board has issued two different RANs for water rents every year since 2000-01, one RAN for garbage fees every year since 2002-03, and one RAN for sewer rents every year since 2000-01.

<sup>13</sup> \$220,000 \* 6 = \$1,320,000

<b>Table 2: RANS</b>				
<b>Type of RAN</b>	<b>Fiscal Year</b>	<b>Original Issue</b>	<b>Interest Paid Through February 28, 2011</b>	<b>Balance as of February 28, 2011</b>
Water Rents <sup>a</sup>	2000-01 or before	\$400,000	\$97,899	\$89,500
Water Rents <sup>a</sup>	2000-01 or before	\$400,000	\$114,059	\$350,000
Garbage Fees	2002-03	\$90,000	\$19,750	\$146,000 <sup>b</sup>
Sewer Rents <sup>a</sup>	2000-01 or before	\$100,000	\$13,456	-
<b>Total</b>		<b>\$990,000</b>	<b>\$245,164</b>	<b>\$585,500</b>
<sup>a</sup> Village officials could not determine the first year the Board issued the water and sewer RANs because the Clerk and Treasurer could not provide documentation prior to 2000-01. <sup>b</sup> In 2009 the Village increased the amount of the garbage RAN.				

Because the Board relied on the use of RANs to finance operating expenditures, Village taxpayers have incurred approximately \$245,000 in interest expense and still have \$585,000 to repay.

Budget for 2011-12 – The Board had adopted a budget for the 2011-12 fiscal year that discontinues the practice of using the FEMA grant line item to inflate revenues beyond anticipated expenditures. However, the Board has instead made unrealistic revenue projections for garbage fees and water rents that could again create a shortfall for the fiscal year.

Garbage fees in the general fund are budgeted to increase by approximately \$50,000 to \$558,000. The Board approved an 8 percent garbage fee increase for 2011-12. Based on 2010-11 revenues, the Village will collect about \$543,000, which will likely result in a shortfall of \$15,000. Water rents are budgeted to be \$3 million in 2011-12. However, the Village only received \$2.5 million in water rents in 2010-11. There has been no rate increase and there are no plans for a rate increase that would justify this budgeted increase.

The Clerk and Treasurer told us that these were budgeting errors on the Board’s part and Village officials did not know how they would affect the current fiscal year.

Due to poor budgeting, the Board has incurred approximately \$245,000 in interest expense to cover cash flow shortages since 2000, and still owes approximately \$585,000 for its ongoing short-term borrowing. By adopting unrealistic revenue projections for 2011-12, the Board faces a potential additional shortfall of approximately \$515,000. Therefore, it is likely that the Board yet again will need to issue RANs to sustain operations, incurring additional interest costs in the process and a potential deficit at the end of the 2011-12 fiscal year.

## Accountability

The Board is responsible for adopting written policies and procedures that describe the accounting records to be maintained, and the guidelines for collecting and depositing amounts due and for advancing moneys from one fund to another. We found that the Board did not establish such written policies and procedures. As a result, the former Treasurer and the current Clerk and Treasurer did not maintain necessary records and/or follow proper procedures for serial bonds, tax receipts or inter-fund loans.

Serial Bonds – It is important for the Clerk and Treasurer to maintain a bond register for open serial bonds to provide assurance that payments are made when due, and for the proper amounts. However, the Clerk and Treasurer did not maintain a bond register. As a result, Village debt was not properly monitored. Due to this control weakness, we reviewed payment and bank records. Although we did not find any significant discrepancies, the failure to properly monitor debt increases the risk of errors and/or irregularities occurring and going undetected.

Tax Receipts – The Village collects taxes from March through October with late penalties assessed on payments after April 2nd, each year. Accounting records for the dates that tax payments are received must be consistent. By law, all payments must be deposited within 10 days of receipt.

The Clerk and Treasurer date stamps tax receipts and copies of tax bills to indicate the dates that payments are received and records the payments on a tax receipt spreadsheet. We reviewed 46<sup>14</sup> tax receipts after April 2nd and found that the dates on 21 of the receipts were not the same as the dates stamped on the copies of the bills. As a result, Village officials could not determine when the payments were made. Furthermore, based on the last stamp date, 12 of the 46 receipts did not have the correct penalties assessed. Eleven receipts had penalties under assessed and one receipt had penalties over assessed, for a combined shortage of \$898. In addition, 15 of the tax receipts were held by the Clerk and Treasurer for over 20 days before being deposited. The failure to deposit collections on a timely basis increases the risk that they could become unaccounted for.

Inter-Fund Loans – General Municipal Law allows the Clerk and Treasurer to temporarily loan moneys held in one fund to another fund to address budget shortfalls when available cash is not sufficient to pay current obligations. The Board must authorize each loan, ensure that suitable records are maintained, and ensure that repayment is

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<sup>14</sup> Only receipts after the penalty date were considered for selection, and the selection within that group was random.

made, with interest, no later than the close of the fiscal year in which the advance was made.

The Village did not follow proper inter-fund loan procedures. The Village bills residents for garbage fees, and sewer and water charges on a single bill. When payments were received all moneys were deposited into the water fund. This inadvertently created inter-fund loans from the general and sewer funds to the water fund because the garbage fees and sewer rents should have been deposited into general and sewer funds. The moneys remained in the water fund for no set period of time. They were periodically transferred from the water fund to the general and sewer funds to address the cash flow deficiencies as they developed in those funds due to operations.

During our audit period, there were 245 transfers among the water, general and sewer funds totaling \$7,534,725. Of these transfers, 173 totaling \$2,073,930 were for payroll, while the other 72 transfers, totaling \$5,460,795 had no indication of their purpose recorded.

The Board did not approve any of these transfers; therefore, the deputy treasurer made the transfers without proper authorization. In addition, no accounting records were kept to indicate if the transfers were intended to be for money due to the general fund for garbage fees, or to the sewer fund for sewer rents, or if they were intended to be advances from the water fund. Furthermore, no transfers were repaid at the end of the fiscal year, and no interest was paid for any of the transfers. Due to the poor recordkeeping, the Clerk and Treasurer cannot easily determine if any moneys are due to other funds, or the financial condition of any of the funds.

## **Wire Transfers**

Effective internal controls over wire transfers include a policy and an agreement with the bank to clearly describe the wire transfer activities the Village will engage in and which employees have the authority to process transactions. Prior approval should be obtained for all wire transfers and transfer requests should not be processed without a call back from the bank to a second employee to verify the accuracy and legitimacy of the transfer requests.

The Village processes all wire transfers online through one bank. The Board has not adopted a policy or entered into a wire transfer agreement with the bank. As a result, the deputy treasurer, who performed all wire transfers during our audit period, completed 83 transfers totaling \$5.8 million without prior approval or a call back verification of the transfer. We reviewed these transactions and did not find any unusual activity (all transfers were between Village owned accounts or for debt payments). However, without a policy

or written agreement, there is an increased risk that inappropriate transfers could occur and go undetected.

## Recommendations

5. The Board should adopt realistic and structurally balanced budgets, using actual financial results from prior years to project future revenues and expenditures.
6. The Board and Village officials should develop a plan to eliminate the fund balance deficit.
7. The Board should review all RANs and take action to satisfy the outstanding balances.
8. The Board should adopt written policies and procedures that require the Clerk and Treasurer and/or deputy treasurer to:
  - Maintain a bond register
  - Ensure that the date stamps on tax receipts and copies of tax bills received are consistent
  - Account for tax penalties due for payments documented as having been received after April 2nd each year
  - Deposit all tax payments within 10 days of receipt
  - Deposit all garbage fees and sewer rents in the appropriate funds
  - Obtain Board approval for all inter-fund transfers, and ensure that the accounting records clearly indicate the purpose for which the inter-fund transfers were made.
9. The Board should review all inter-fund activity and calculate the net amounts due to and due from each fund. All amounts should then be repaid with interest.
10. If it becomes necessary to advance moneys between funds in the future, the Board should specifically authorize each advance, ensure that suitable records are maintained, and ensure that repayment is made with interest no later than the close of the fiscal year in which the advances are made.
11. The Board should adopt a policy and enter into a written agreement with its bank to:

- Describe the types of wire transfer activities the Village will engage in
- Identify the employees that have the authority to process wire transfers
- Ensure that no wire transfers are made without prior approval and a call back to a second employee to verify the accuracy and legitimacy of the transfer requests.

## Information Technology

The Village relies on an information technology (IT) system for many essential functions including user and taxpayer billings, Internet access, email communication, payroll and non-payroll disbursements, financial records, and reporting to State and Federal agencies. Therefore, the IT system and the data it holds are valuable resources. If the IT system fails or is damaged, the resulting problems could range from inconvenient to severe. Even small disruptions can require extensive time and effort to evaluate and repair. The Board is responsible for establishing policies and procedures to protect the Village's computer equipment, software, and data. These include a security assessment that identifies, prioritizes, and minimizes data security risks, and guidelines for disaster recovery, acceptable use and remote access. In addition, backups of electronic data should be run and tested on a routine basis, and stored in a secure off-site location.

The Board did not adopt guidance for assessing the IT system for vulnerabilities, disaster recovery or acceptable use. In addition, remote access was granted to four users despite a lack of procedures to monitor their activities and there was no IT administrator until July 2010 which resulted in backups of Village data not being tested. As a result, the Village has permanently lost valuable information and data. As of July 2010, the Village has entered into an inter-municipal agreement with the Town of New Windsor for IT services.

### **Policies and Procedures**

The Board must adopt IT policies and establish control procedures. Every policy adopted by the Board should be understood by all Board members, customized to fit the unique needs of the Village, reviewed periodically and updated when necessary. Adopted policies must be effectively communicated to those in the Village that use the IT system to be effective.

The Board neglected to adopt any IT related policies. As result, there are significant control weaknesses in the Village's IT operations that could result in lost data.

Security Assessment – A formal written security plan serves to document the process for evaluating security risks, identifying and prioritizing the more vulnerable areas, and documenting the measures Village personnel must take to minimize and monitor such risks. For example, a security plan may call for classifying types of data according to their sensitivity, documenting the classification levels and specifying which officials, employees, and vendors are allowed access to each level.

The Board has not developed a written security plan to document any processes that are currently followed or the procedures that may already be in place. Without a well-developed, written security plan, there is an increased risk that policies and procedures that are already in place may not address all vulnerable areas and therefore may not be effective.

Disaster Recovery – An effective disaster recovery plan identifies critical system functions and describes the steps that Village personnel should take to restore essential operations in the event of a disaster. Such disasters include any sudden, catastrophic event (e.g., fire, computer virus, power outage, or inadvertent employee action) that compromises the integrity of the IT system and data. An effective plan should also include measures that focus on disaster prevention.

The Board has not established a formal disaster recovery plan. Therefore, Village personnel have no procedures to prevent or minimize the loss of equipment and data and no guidelines for implementing data recovery procedures and resuming critical operations as efficiently as possible. As a result, in the event of a disaster, the Village is at risk of not being able to perform essential operations such as payroll and vendor payments.

Acceptable Use – An acceptable use policy defines the Board’s goals for the use of equipment and computing systems, and the security measures to protect resources and confidential information. The policy should address the acceptable use of email accounts, Internet access, and the installation of software onto Village computers. It is important that the policy include provisions for enforcement and that system users provide acknowledgement that they are aware of, and abide by, the policy.

The Board has not adopted an acceptable use policy. We tested four<sup>15</sup> of the Village’s 10 computers. Although we did not find any major unusual or suspicious activities, the lack of an acceptable use policy increases the risk that the IT system could be used for non-Village purposes.

Remote Access – Effective internal controls ensure that remote access (the ability to access a computer from the Internet or other external sources) is controlled and monitored so that only authorized individuals may enter or retrieve data. Such controls include policies and procedures addressing how remote access is granted, who is given remote access, and security issues such as how remote access will be monitored.

---

<sup>15</sup> All four were in the finance/business area (the Clerk and Treasurer, the payroll clerk, the former Treasurer and the Mayor).

The Village did not have a remote access policy. Remote access was granted to the Clerk and Treasurer, the deputy treasurer, the water clerk, the IT administrator from the Town of New Windsor, and the financial software vendor. The remote users had unlimited access to the system. In addition, no one ran available logs to review and monitor the activity of remote users after they entered the system. As a result, there is a risk that computerized data could be compromised and that unauthorized activity could go undetected.

The adoption of policies and/or procedures for security, disaster recovery, acceptable use and remote access do not guarantee the safety of the Village's computer system or the electronic information it has been entrusted with by taxpayers, customers, employees and others. However, the lack of such guidance significantly increases the risk that data, hardware and software systems may be lost or damaged by inappropriate access and use.

## **Backup Data**

Sound business practices require that backups of the Village's electronic data be made so that it can be restored in the event of loss. Backup data should be kept in a secure alternate location and routinely tested to ensure its integrity.

At the beginning of our audit period, the Village did not have an IT administrator and, therefore, backups of the Village's data were not made. The system crashed in June 2010 and all information with the exception of the financial data was lost. The Village has not been able to retrieve this data, which includes documents such as Board minutes and spreadsheet applications.

As a result of these control deficiencies, the Village has permanently lost valuable information and data. In July 2010, the Village entered into an inter-municipal agreement with the Town of New Windsor for IT services including the nightly backup of Village data. The Village's data is now backed up and stored at an off-site location and is routinely tested to ensure its integrity.

## **Recommendations**

12. The Board should adopt a comprehensive security plan, a disaster recovery plan, an acceptable use policy and a remote access policy. These plans and policies should be reviewed periodically and updated when necessary.
13. The Board should ensure that all system users are aware of and abide by the acceptable use policy.
14. The Board should evaluate the needs of the employees and vendors who have remote access and limit such access to only those who require remote access to perform their duties.

15. Village officials should run available logs, monitor remote access and investigate any unusual activities.
16. The Board should ensure that the duties of an IT administrator are assigned at all times.
17. Village officials should periodically verify that backups are run and tested in accordance with the inter-municipal agreement.

## **APPENDIX A**

### **RESPONSE FROM LOCAL OFFICIALS**

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

We received two attachments from Village trustees which we did not include with the Village's response. It is the Office of the State Comptroller's policy to request a single response, and to include this response in our final report. Therefore, we have included only the letter we received from the Mayor, the Village's chief executive officer, as the Village's response. This response adequately addresses the Village's concerns related to this audit.

The Village's response letter refers to page numbers that appeared in the draft report. The page numbers have changed during the formatting of this final report.

*The Village of Cornwall-on-Hudson*

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Dec. 29, 2011

Christopher J. Ellis  
Chief Examiner  
Office of the State Comptroller  
Newburgh Regional Office  
33 Airport Center Drive, Suite 103  
New Windsor, NY 12552

Dear Mr. Ellis:

I write in response to the draft audit of Selected Financial Activities of the Village of Cornwall-on-Hudson.

I appreciate the opportunity for Village Clerk Jeanne Mahoney and me to meet Dec. 14 with [REDACTED] and [REDACTED] to discuss the report. Most of my comments reflect points that the clerk and I made during that meeting. I have also included comments from the Deputy Mayor and trustees as attachments 1 and 2.

In the Scope and Objectives section of the Executive Summary, I suggest that it incorporate a simple timeline of your office's activities, including when the report was begun and ended (the report does mention the May 18, 2011 end-of-fieldwork date under Financial Operations); why the audit was undertaken; and who was interviewed. The report should note that the issues discussed took place before I became mayor in April 2011 and before Jeanne Mahoney became treasurer in April 2011. Adding these elements will strengthen the report's context and will facilitate understanding the points of view presented.

See  
Note 1  
Page 24

Throughout the report, Jeanne Mahoney is mistakenly referred to as the Clerk-Treasurer; she has two titles, Clerk and Treasurer. In the Background section of the Introduction, the report erroneously states that the Village Board served as the COHLDC ([REDACTED] acknowledged this error in our Dec. 14 meeting).

See  
Note 2  
Page 24

**Public Works Building**

While I understand the content of this section, I find the choice of words inflammatory and irresponsible. Beginning in the Audit Results section of the Executive Summary, the phrase "circumvented applicable State laws" and in Public Works Building section, "to avoid compliance with State Laws," not only fail to state the true intent of using a local development corporation – to save taxpayer dollars, they malign Village Board members, and the village taxpayers who served on the LDC. In addition, the report contains contradictory statements: On page four, the report states "did not act in the best interest of the Village taxpayers," whereas on page 10 it states "may have expended funds not in the best interest of taxpayers."

See  
Note 3  
Page 24

See  
Note 4  
Page 24

*The place of which Henrick Hudson said in 1609: "A Very Pleasant Place To Build A Towne On"*

While the report states that the public works building is not being used, it makes no reference to the village's efforts to bring the building up to code and use it, and to see if anyone can be found liable to pay for renovations. Recommendation #3 (having "an engineer review the apparent deficiencies of the DPW") has been underway during the course of the audit. I have asked the attorney for the village to finalize the dissolution of the local development corporation (Recommendation #4).

See  
Note 5  
Page 25

### **Financial Operations**

We have begun addressing the concerns mentioned in the report. For instance, we approve a Warrant at our monthly business meeting; we approve transfers before they occur; we have significantly decreased our RANs; and we have begun to explore separate billing for sewer rents.

While the report mentions that the 2010-11 books and records had not been closed, it should say why: The village did not undertake an audit for three years. Since becoming mayor, I have contracted for outside audits of the Village's financial statements and received a compilation for 2008-09, an audit for 2009-10 and a compilation for 2010-11 (the books are in the process of being closed).

See  
Note 6  
Page 25

Regarding Recommendation #5 ("adopting realistic and structurally balanced budgets"): The 2012-13 budget I, as budget officer, proposed is balanced and realistic. I have not included the FEMA grant as part of the Village's revenue (page 15 of the report erroneously states that the 2011-12 budget, prepared by then treasurer Stephen Auffredou, discontinued the practice of using a FEMA grant).

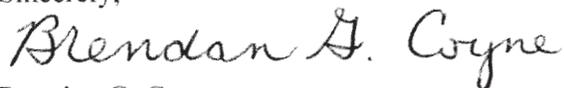
Regarding Recommendation #6 ("eliminate the fund balance deficit"): I believe the recommendation should go further and recommend maintaining a healthy fund balance.

### **Information Technology**

I acknowledge that the Village needs policies regarding information technology. The Village Board will follow the report's findings and institute policies as recommended.

Thank you for your research and recommendations. We have already implemented some of the recommendations and we will prepare a written, corrective action plan within 90 days of your final report.

Sincerely,



Brendan G. Coyne  
Mayor

## APPENDIX B

### OSC COMMENTS ON THE VILLAGE'S RESPONSE

#### Note 1

The Executive Summary and the Introduction sections of our report clearly describe the audit scope and objectives. In addition, the Methodology section (Appendix C) explains, in detail, the steps we took in our audit process, including those we interviewed. We audited the financing and construction of the Village's Department of Public Works (DPW) building, the Village's financial operations, and the Village's information technology (IT) systems.

#### Note 2

We have revised the report to state "Clerk and Treasurer. "We also removed the statement "the Village Board served as the Cornwall-On-Hudson Local Development Corporation (COHLDC) Board" from the report.

#### Note 3

We based our statements and conclusions on documents and information provided by Village officials and employees. In a memorandum dated August 20, 2007 from the Village Attorney to the Village Board, the following was stated in reference to "Why form an LDC?"

*"While local governments may undertake many economic development activities themselves, there remain Constitutional and state statutory provisions that restrict municipalities' abilities to function in this area. In addition to those constraints, municipalities are also limited by competitive bidding requirements, the Wicks Law, etc. The constraints often make it impractical for local government to implement economic development plans or programs effectively. Because LDCs are not "political subdivision," they are not subject to competitive bidding requirements, the Wicks law."*

Furthermore, in the same memorandum explaining why the COHLDC was used to construct the DPW building, the Village Attorney stated:

*"To maximize the economics and make the project affordable, we required utilization of the LDC as the legal entity that would be able to accomplish the project without having to deal with the extra costs associated with the WICKS law."*

We interpreted these statements to mean that the Village used the COHLDC to build the DPW building to avoid complying with the WICKs Law and competitive bidding requirements, which are State laws.

#### Note 4

In the Executive Summary, we stated that the Board did not act in the best interest of Village taxpayers when it avoided complying with applicable State laws by using the COHLDC to construct the DPW

building. Had the Board not used the COHLDC it would have had to comply with all applicable laws and requirements, and in all likelihood the outcome of the DPW building would have been different.

In the Public Works Building section (p. 8), we stated that, without proper planning and without seeking professional advice on the use of questionable land, the Board may have expended funds not in the best interest of taxpayers. If the Board had properly planned and sought professional advice on the use of the land, the building might have been constructed properly or not at this site.

#### Note 5

We applaud Village officials' efforts to bring the building up to code. These efforts occurred after the completion of our field work.

#### Note 6

Under the financial operations section of the report, we cited poor recordkeeping as a contributing factor in the Village officials' inability to close the Village's books and records.

## APPENDIX C

### AUDIT METHODOLOGY AND STANDARDS

To accomplish our audit objectives, we interviewed Village officials, Board members and employees, tested records and examined documents. Our procedures included the following:

- We obtained all documentation available from Village officials concerning the DPW building, including Board minutes, lease agreements, inter-office memorandums, email communications, sale of property contracts, bond documentation, canceled checks, the COHLDC check register, and Board resolutions.
- We contacted the Town of Cornwall tax assessor to obtain an appraisal of the DPW property and building.
- We obtained an understanding of the internal controls related to budget development by interviewing Village officials and Board members and reviewing Board minutes.
- We analyzed changes in fund balance of the general, water and sewer funds for the 2008-09 through 2010-11 fiscal years.
- We reviewed all available documentation for revenue anticipation notes going back to 2000, the oldest documentation officials could provide for us.
- We examined all bond documentation, including prospectuses, when available, payments for bond debt including canceled checks and wire-transfers, and bank statements.
- We examined tax payment receipts, tax rolls, tax warrants, duplicate tax invoices, deposit slips and bank statements.
- We reviewed billing and deposit records for garbage fees, water charges and sewer charges, and reviewed moneys transferred between funds.
- We reviewed all bank statements for our audit period to trace inter-fund transfers.
- We interviewed Village employees and Town of New Windsor IT personnel to gain an understanding of the IT environment and procedures in place.
- We performed audit software tests on four Village computers.

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

## APPENDIX D

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