



Sullivan County Industrial Development Agency

PILOT Program

Report of Examination

Period Covered:

January 1, 2012 — April 10, 2013

2013M-161



Thomas P. DiNapoli

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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

August 2013

Dear Agency Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board 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 Sullivan County Industrial Development Agency, entitled PILOT Program. 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 recommendation are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

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

Introduction

Background

Industrial Development Agencies (IDA) are independent public benefit corporations whose purpose is to promote, develop, and assist industrial, manufacturing, warehousing, commercial, research, and recreation facilities. The overall goal of IDAs is to advance the job opportunities, health, general prosperity, and economic welfare of the people of the State.¹ Typically, projects that receive IDA benefits involve the acquisition, construction, or major renovation of buildings or other structures and generate short- and long-term employment in construction and operation-related jobs.

The Sullivan County Industrial Development Agency (SCIDA) was established in 1970 and is governed by a Board comprising nine members appointed by the Sullivan County Legislature. The Board is responsible for the general management and control of SCIDA's financial and operational affairs. SCIDA appointed an Executive Director to manage its day-to-day operations, and maintains Chief Executive Officer and Chief Financial Officer positions.

SCIDA extended benefits totaling approximately \$7.1 million for 58 projects during our audit period. These benefits were in the form of reducing the taxes the projects would have paid if the projects occurred without assistance. SCIDA generally assumes the title of the real and/or personal property owned by the businesses that are involved in SCIDA's approved projects, which allows SCIDA to offer benefits to these businesses (e.g., sales tax exemptions and real property tax abatements). SCIDA is not required to pay taxes or assessments on any property that it acquires or that is under its jurisdiction, control, or supervision. SCIDA provides a general Payment in Lieu of Taxes (PILOT) agreement to approved businesses, which results in real property tax abatements for the business owners.

PILOT agreements are governed by SCIDA's Uniform Tax Exemption Policy (UTEP), which outlines, among other things, the process of recapturing benefits if a company receiving a PILOT does not meet anticipated performance. These projects reportedly created 2,188 new jobs, in addition to retaining 612 existing positions. The projects also paid \$4.2 million in PILOTs, which were disbursed to the taxing jurisdictions in which the projects were located. This resulted in a net benefit to the PILOT projects (after PILOT payments) of \$2.9 million. The improvements made during the projects will also increase the long-term property assessment values, resulting in an increased tax base for each taxing jurisdiction involved.

¹ The powers and duties of IDAs are set forth in General Municipal Law.

Objective

The objective of our audit was to review the SCIDA PILOT Program. Our audit addressed the following related question:

- Did the Board design and implement an adequate system to select, monitor, and manage benefits and incentives granted to firms or businesses within the SCIDA PILOT program?

**Scope and
Methodology**

We examined the PILOT Program documentation of SCIDA for the period January 1, 2012, to April 10, 2013.

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 is included in Appendix C of this report.

**Comments of
Local Officials and
Corrective Action**

The results of our audit and recommendation have been discussed with SCIDA officials and their comments, which appear in Appendix A, have been considered in preparing this report. Except as specified in Appendix A, SCIDA officials generally agreed with our recommendation and indicated that they have taken or plan to take corrective action. Appendix B contains our comment on issues raised in SCIDA's response.

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 Executive Director's office.

Payment in Lieu of Taxes (PILOT) Program

Each IDA typically establishes its own individual project criteria based on the economic needs and goals of the community it serves. Such criteria can help ensure that all project applications are measured against the same standards. For example, in addition to the period of the real property tax exemption, the percentage of exemption, and the types of projects for which exemptions can be claimed, criteria could include (but not necessarily be limited to) the extent to which the proposed project will create or retain permanent, private-sector jobs, provide additional sources of revenue for municipalities and school districts, affect other businesses or economic development projects, or require additional infrastructure services.

To accomplish agency goals, the Board should establish a system that effectively selects projects for PILOT programs in order to provide the most beneficial impact on the community. The Board should create and maintain a Uniform Tax Exempt Policy which provides the Board with detailed procedural guidelines to make project approval or denial decisions. The UTEP should include specific criteria for evaluating each project application based on the community's needs. IDA officials should verify the information on project applications and prepare a cost-benefit analysis of each prospective project to help support their decision to either approve or deny the project application. Further, the Board should ensure procedures are in place to identify and disclose all agency members' financial interests in potential projects in compliance with its Code of Ethics policy. Lastly, IDA officials should ensure that each project is closely monitored to verify that the benefiting businesses are following the policies and meeting established goals. Whenever possible, the Board should manage the projects by adjusting the benefits provided based on the project's performance in relation to the established goals and criteria.

SCIDA has established a UTEP for both general and specific-purpose projects. The policies are specific and clearly articulate project goals and abatement schedules. The project approval process includes in-depth cost-benefit analyses based on reasonable assumptions. However, there is no effective mechanism in place to identify SCIDA members' financial interests in potential projects during the selection process. Projects are monitored and performance goals are tracked. PILOT amounts are adjusted annually based on performance.

Selecting Projects

As part of its process for approving or denying PILOT assistance to project applicants, the Board should determine if any SCIDA officials would have a financial interest in the potential project. To this end, SCIDA officials should comply with the SCIDA's Code of Ethics policy and complete financial disclosure forms to be filed with the County. A review of these forms and adherence to policy requirements would help the Board select projects that do not create even the appearance of impropriety. Further, SCIDA officials should prepare a cost-benefit analysis for each proposed project based on the information provided in the application, to include all costs associated with the project and any expected benefits to the community. After completing the cost-benefit analysis, they must compare it to the business owner's submitted application and SCIDA's UTEP criteria. A proper cost-benefit analysis provides a basis for comparing the requested assistance with future benefits the applicant intends to produce for the community.

Although SCIDA has a Code of Ethics policy,² there is no effective mechanism to verify that Board members are adhering to it. Although SCIDA officials submit a financial disclosure form to the County Clerk of the Legislature detailing any business interests, this form is sealed. According to the Clerk of the Legislature, the County does not unseal and review the financial disclosure forms or provide them to the SCIDA for review. SCIDA officials told us the reliance on these financial disclosures filed with the County is the only method in place, aside from Board members volunteering such information, to determine if any officials have an interest in potential projects.

One of the projects in our review was approved for a PILOT agreement even though a SCIDA Board member was the spouse of one of the two partners in the potential project. The signed project application³ included a section asserting that no member, officer, or employee of SCIDA has an interest, whether direct or indirect, in any transaction contemplated by this application. At our request, the Clerk of the Legislature provided the financial disclosure forms for this SCIDA Board member to us. In both instances, these forms would not have allowed SCIDA officials to determine whether a financial interest existed prior to project approval because they were sealed and never reviewed.

² The policy states: "No director, officer, or employee of the Agency shall engage in any transaction as a representative or agent of Agency with any business entity in which he or she has a direct or indirect financial interest that might reasonably tend to conflict with proper discharge of his or her official duties."

³ The application was signed by the SCIDA Board member's spouse who is a 50 percent owner in the project that was granted a PILOT.

We also reviewed the applications of 10 sample projects, including the project in which the Board member's spouse shared ownership of the project company, and determined that comprehensive cost-benefit analyses were completed for all 10 projects⁴ to assist and support the decisions to approve SCIDA benefits. The cost-benefit analysis and criteria for approval of the project in question were consistent with those of the other sampled projects. We also verified that the data provided for all 10 projects was sufficient to perform an effective analysis of the costs and benefits of the project as they related to the affected local municipalities. However, without an effective method of determining whether SCIDA officers have any financial interest in a potential project, there is an increased risk of the appearance of impropriety.

Monitoring and Managing Projects

After selecting a project for benefits, it is imperative to monitor its performance and effectiveness to ensure that both the contractual requirements for construction and improvements to new or existing property and the intended job goals are being met. Whenever possible, PILOT agreements should include provisions for SCIDA to address shortcomings of timelines or goals that the projects are contractually obligated to meet. SCIDA officials should address any variations between actual performance and the contractual requirements.

SCIDA officials were holding project owners to the contractual stipulations for the PILOT agreements we tested. We reviewed five⁵ PILOT agreements that required job creation or retention, for which adjustments made to PILOT payments totaled approximately \$230,000 in increased benefits to the local municipalities over a five-year period. The officials made these adjustments after verifying, on an annual basis, that those projects with contractual job requirements maintained the agreed-upon job levels. These adjustments reflect an active monitoring and management process that SCIDA performs to protect the interests of the local municipalities where the PILOT projects are located.

SCIDA projects have also been successful at increasing the long-term tax bases of the corresponding taxing municipalities. Of three⁶ sampled projects, the cumulative PILOT payments over the terms of the agreements would net the associated taxing jurisdictions nearly

⁴ Eight of the projects' cost-benefit analyses were completed by a contracted third party, one analysis was done by SCIDA staff using specialized software, and one project was a continuation of a prior project in which actual results served as a cost-benefit analysis.

⁵ The five selected projects within our scope period were those that should have had a penalty assessed based on a failure to meet agreed-upon job creation goals.

⁶ We selected three of the 10 most recently approved IDA projects.

\$973,000 more than the real property tax revenues would have been if no projects or improvements occurred at the property locations.⁷

Table 1: PILOT Benefits to Taxing Municipalities^a			
Project	Estimated Real Property Tax Revenue During PILOT Term	Estimated PILOT Payment Revenue During PILOT Term	Net Benefit from PILOT Program
Catskill Distilling	\$154,549	\$279,268	\$124,719
MG Catskills LLC	\$49,883	\$665,735	\$615,852
PTNY (Plastic Technologies of New York)	\$444,365	\$676,594	\$232,229
Total	\$648,797	\$1,621,597	\$972,800
^a Rounded to nearest dollar			

Because PILOTs are calculated based on the tax abatements to the improvement value of the project properties, those payments are consistently larger than the property tax payment on the unimproved property.

We also estimated that the improvement value of the three sampled projects totaled \$1.4 million, which will increase the tax assessment of these properties and generate significant tax revenues in future years after the conclusion of the PILOTs. The local municipalities' increased assessed value provides for further taxing power in future years and also has the potential to lower the municipalities' overall tax rates. At the end of the PILOT terms, these projects will pay full taxes and provide revenues to the municipalities that may not have been available otherwise. For example, the most recently completed PILOT project had an assessed value on the vacant parcel of land of approximately \$35,000 prior to the project start. At completion, because of the improvements made as part of the project, the assessed value of the property had increased to over \$5.57 million. This increase in assessment will effectively lower the tax rates of the taxing jurisdictions in which the property lies, resulting in lower property taxes for other parcels within those jurisdictions.

Recommendation

1. SCIDA officials should improve their current process for identifying SCIDA officials' potential financial interests in projects seeking SCIDA assistance. Such improvements could include, but are not limited to:

⁷ Net amounts to taxing jurisdictions are based on projected real property tax payments at the pre-improvement assessed property values and a projected annual tax rate growth of 2 percent.

- Asking the County to provide a copy of all financial disclosure forms received from SCIDA officials
- Updating the SCIDA UTEP to include a provision requiring any Board member that may have the appearance of a financial interest in a project to publicly disclose the interest at a SCIDA Board meeting, to be documented in the meeting minutes
- Ensuring that the adopted Code of Ethics policy provisions are monitored and complied with by all SCIDA officials.

APPENDIX A

RESPONSE FROM LOCAL OFFICIALS

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

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August 19, 2013

[REDACTED]
Division of Local Government
And School Accountability
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RE: Combined Audit Response and Corrective Action Plan
Sullivan County Industrial Development Agency
Audit Report Title: PILOT Program, Report of Examination
Audit Report Period: January 1, 2012 – April 10, 2013
Audit Report Number: 2013M-161

Dear [REDACTED]

Please accept this letter as the Sullivan County Industrial Development Agency's ("SCIDA") combined response and corrective action plan to the Draft Audit Report referenced above. We appreciate the external audit of our PILOT program and are pleased to accept its findings that SCIDA's projects are (i) selected based upon comprehensive cost-benefit analyses and clearly articulated policies setting forth project goals and abatement schedules, (ii) actively monitored for performance and (iii) annually adjusted to match PILOT payment obligations to the agreed-upon job levels thereby eliminating the need for recapture of benefits on underperforming projects. Furthermore, we agree with the findings that SCIDA projects have been successful at increasing the long-term tax bases of the corresponding taxing municipalities. However, we have identified the following items that require factual corrections or clarifications:

(1) On page 4 of the report it states that SCIDA extended benefits totaling approximately \$7.1 million for 58 projects during the audit period. Although the following paragraph correctly includes a statement that the same projects paid \$4.2 million in PILOT payments, it is vital for any reader to understand that the actual amount of property tax abatement granted by SCIDA was \$2.9 million. The fact that the \$7.1 million represents the full assessed value of the property

See
Note 1
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and not the difference between the full assessed value and the amount the projects pay in PILOT payments exaggerates the degree to which SCIDA offered property tax abatement benefits. Therefore, these statements should be clarified in order to not mislead the reader.

(2) We understand that the report is written in a style that first introduces the best-practices for what Industrial Development Agencies (“IDA”) should be doing to properly administer PILOT programs and then reports on the specifics of SCIDA’s PILOT program. However, based upon the wording of the report, the reader can easily misinterpret the statements regarding what should be done by IDA’s as a statement that SCIDA is not doing such, when in fact the report found SCIDA to be implementing the stated best-practices. One example in particular, on page 6, the report states “[F]urther, SCIDA officials should prepare a cost-benefit analysis for each proposed project based on the information provided in the application, to include all costs associated with the project and any expected benefits to the community.” Although in the immediately preceding paragraph, the audit clearly found that SCIDA’s project approval process included in-depth cost-benefit analyses based upon reasonable assumptions. Thus, the report should be clarified in order to avoid misunderstandings by the reader.

(3) On page 7, the statements regarding the financial disclosure filings of an SCIDA board member are misleading. The wording of such statements implies that the board member’s 2011 and 2012 financial disclosure forms were filed late when in fact both filings were timely. All filings for any given year are due on May 1st of the following year. For example, the filing that applied to calendar year 2011 was due May 1st, 2012. In addition, pursuant to Sullivan County’s local procedures, an extension on a federal tax return automatically extends the financial disclosure filing date to October. The report states that the board member’s 2011 disclosure was filed in April of 2012 and the 2012 disclosure was filed in May of 2013. Therefore, both disclosure were timely filed even though the auditors requested the 2012 disclosure prior to the filing due date. Thus, these misleading statements should be clarified in order to reflect the actual facts.

See
Note 1
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The SCIDA accepts the audit recommendation that it should improve its current process for identifying SCIDA officials’ potential financial interest in projects seeking SCIDA assistance. Toward that end, the SCIDA will implement the following corrective action plan:

First, SCIDA will engage outside counsel to prepare a memorandum of law on the numerous ethical rules applicable to volunteer IDA board members, which will include an executive summary presenting key provisions. The memorandum of law will address, reconcile and condense the numerous ethical provisions contained in the General Municipal Law, the Public Authorities Accountability Act, the newly enacted Sullivan County Ethics Law, SCIDA’s current policy, opinions of the Attorney General’s Office and the Comptroller’s Office, and case law.

Secondly, SCIDA will require all board members to participate in mandatory training focused solely on ethical rules and considerations.

Lastly, SCIDA will revise its application to include a more accurate and detailed ethics disclosure statement. The applicant will be required to certify that they have read, understood and inquired into any ethical conflicts and certify that they have none.

SCIDA is strongly committed to its mission and is pleased to have the success of its PILOT program recognized in this audit. SCIDA's success is the direct result of its dedicated staff and the volunteers that serve on its board, all of whom constantly strive to improve SCIDA's performance. As a result, SCIDA welcomed the audit and was open to any recommendations for improvement, which resulted in the proposed plan as set forth above.

We look forward to receiving the final audit report.

Sincerely,

Ira Steingart
Chairman of the Board

cc: IDA Board Members
Allan C. Scott, CEO
Jennifer Brylinski, Executive Director
Walter F. Garigliano, Esq., Agency Counsel

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APPENDIX B

OSC COMMENT ON THE LOCAL OFFICIALS' RESPONSE

Note 1

We have modified the report to address this concern.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

To accomplish the objective of this audit and obtain valid evidence, our audit procedures included the following:

- We reviewed Article 18-A of General Municipal Law to determine the powers vested in industrial development agencies and the process used to exercise those powers.
- We reviewed SCIDA's UTEP and determined provisions applying to our audit work, specifically regarding the selection, monitoring, and management of PILOT projects.
- We identified the 10 most recent PILOT projects and reviewed a sample of three cost-benefit analyses from PILOT project documentation to determine if they met all applicable requirements, if they were adequately thorough, and if all calculations and assumptions were correct and reasonable. We then reviewed the cost-benefit analyses of the remaining seven PILOT projects to verify they were generally consistent with the three in-depth reviewed analyses.
- We compared the names of SCIDA officials with PILOT program documentation to identify any potential conflicts of interest. We asked SCIDA officials about the policies and procedures regarding potential conflicts of interest. We also reviewed and gained an understanding of the SCIDA Code of Ethics policy. We asked the Sullivan County Clerk of the Legislature about the policies and procedures related to financial disclosure forms and reviewed selected 2011 and 2012 financial disclosure forms to determine if any potential conflicts of interest were identified on the forms.
- We inquired about the project monitoring process with SCIDA officials and assessed it for reasonableness and effectiveness, including the PILOT payment adjustment process. We reviewed PILOT agreements, UTEPs, and PILOT billings to re-calculate and verify the accuracy of adjustments.
- For a sample of five PILOT projects, we completed a five-year historical adjustment review in order to determine the net effect on the associated taxing jurisdictions. We selected for testing projects that failed to meet job goals, which, therefore, should have had a penalty assessed.
- For three of the 10 most recently approved PILOT projects, we calculated an estimated projection for PILOT payments and real property tax payments over the terms of the PILOTs. We then compared the cumulative real property tax and PILOT payment amounts to determine the overall effect of the PILOTs by the time of completion.
- We obtained and compared the assessed property value of the most recently completed PILOT project to document the overall effect on the property's taxable value.

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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