



City of Utica

Financial Controls in the City Comptroller's Office and Information Technology

Report of Examination

Period Covered:

April 1, 2007 — January 31, 2009

2009M-107



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State of New York Office of the State Comptroller

Division of Local Government and School Accountability

July 2009

Dear City Officials:

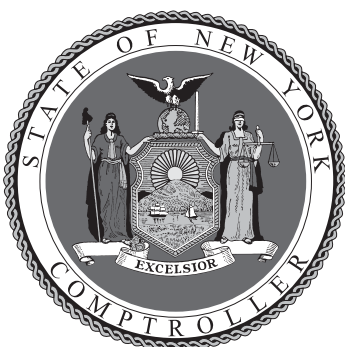
A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments 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 Common Council 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 City of Utica, entitled Financial Controls in the City Comptroller's Office and Information Technology. 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

EXECUTIVE SUMMARY

The City of Utica (City) encompasses approximately 16 square miles in Oneida County and has a population of about 61,000. The City is governed by its Charter and other general laws of the State of New York. The Common Council (Council), which consists of ten members, has overall responsibility for the City's operations. The Mayor serves as the chief executive officer and the Comptroller serves as the chief fiscal officer of the City. The City provides a variety of services to its residents including police and fire protection, sewer utilities, and parks and recreation programs.

The City's operating expenditures are funded primarily with revenues from real property taxes, sales taxes, sewer receipts, and State and Federal aid. For the 2009 fiscal year, the City budgeted expenditures that totaled \$62.5 million for the general fund.

Scope and Objective

The objective of our audit was to determine if the City has established effective internal controls over the financial operations of the Comptroller's Office and information technology for the period April 1, 2007 to January 31, 2009. Our audit addressed the following related questions:

- Have adequate internal controls been established over the financial operations of the City Comptroller's Office to ensure that City assets are properly safeguarded?
- Are internal controls over the City's information technology (IT) system appropriately designed to protect electronic data?

Audit Results

The Comptroller has not adopted comprehensive written policies and procedures to provide guidance and internal controls for payroll processing, claims processing, wire transfers and cash receipts. This lack of guidance has resulted in a lack of segregation of duties and a lack of compensating controls over certain key aspects of the City's financial operations.

The Comptroller did not adequately segregate duties over payroll or provide adequate oversight. Three employees in the payroll department have full access to the computerized payroll records and are able to make changes to salaries, pay rates or hours worked, and their duties are performed with minimal oversight. The City's computerized financial system is able to generate audit logs that show all changes that are made to the payroll application; however, supervisory personnel do not generate or review the available reports. We tested the accuracy of 20 employees' gross pay totaling about

\$913,000 during the 2007-08 fiscal year and found that eight employees did not receive the correct gross pay, resulting in overpayments and underpayments totaling \$5,702 and \$604, respectively. Additionally, our tests of leave accrual records for 20 employees in the 2007-08 fiscal year disclosed that four employees had compensatory leave time balances (valued at \$3,253) in excess of the 30-day maximum accumulation established by their collective bargaining agreements as of March 31, 2008. We also found 20 posting errors in the leave records, resulting in overstatements in leave time balances of \$1,567 and understatements totaling \$1,198. Inadequate controls and a lack of proper oversight increases the potential for errors, fraud and abuse and the risk that individuals may receive compensation and benefits to which they are not entitled.

The City's internal control system does not provide an independent claims audit function, nor does it provide for the adequate segregation of duties. As a result, City officials do not have adequate assurance that all payments are for valid City expenses. Two individuals in the Comptroller's Office are responsible for the entire claims payment function, including processing, approving and paying claims. Our tests of 40 claims totaling about \$2.38 million disclosed four payments totaling approximately \$100,400 that did not contain adequate supporting documentation; however, City officials subsequently provided supporting documentation for \$90,000 of these payments.

City officials have not designed adequate internal controls over wire transfers. There are no documented policies or procedures to identify the process to be used for authorizing, initiating, documenting, reconciling or monitoring wire transfers. One employee in the Comptroller's Office is primarily responsible for performing and recording internal and external wire transfers with little oversight. Our testing of approximately \$34.2 million of wire transfers made in October 2008 disclosed no improper transfers; however this lack of monitoring may lead to incorrect or inappropriate transactions.

With respect to cash receipts, we found that cashiers in the Comptroller's Office have the ability to change the effective date of the tax receipts in the financial system to avoid recording a penalty for payments received after the penalty free period. The City has no controls in place to ensure that these date changes are proper. The cashiers did not document any reason for changing the effective date for these receipts and supervisory approval is not required. We reviewed 250 recorded tax payments for the period of May 6 through May 9, 2008 totaling about \$163,400 and found that 107 payments totaling about \$60,700 were back-dated to reflect an April 30, 2008 receipt date and no late fees were recorded. The late fees for these payments would have been about \$3,000.

Additionally, the Comptroller has not provided written guidance to departments on the time and manner in which moneys should be reported and remitted to the Comptroller's Office. The Comptroller also has not established a control system for departments to issue serially press numbered receipts. We tested 50 interdepartmental remittances totaling \$73,287 and found that the moneys were recorded and deposited in the bank by the Comptroller's Office in a timely manner. However, we found that two departments remitted \$388.50 to the Comptroller's Office without any other documentation and another department submitted \$408 more to the Comptroller's Office than the supporting receipts showed were collected. We were unable to confirm four remittances from the Youth Bureau totaling \$1,360, because the department sometimes completed two separate receipts for the same cash collection.

Finally, City officials have not sufficiently addressed the safeguarding of computer data to ensure proper protection. The Council has not adopted comprehensive policies and procedures relating to all key aspects of the City's IT operations, including but not limited to, physical security, user access,

back-up data and disaster recovery. As a result, there is a greater risk that unauthorized users could gain access to the IT system and that the City could lose important financial data or suffer a serious interruption to City operations in the event of a disaster.

Comments of Local Officials

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials disagreed with certain aspects of our findings and recommendations in our report, but indicated that they planned to implement some of our recommendations. Appendix B includes our comments on the issues raised in the City's response letter.

Introduction

Background

The City of Utica (City) encompasses approximately 16 square miles in Oneida County and has a population of about 61,000. The City is governed by its Charter and other general laws of the State of New York. The Common Council (Council), which consists of ten members, has overall responsibility for the City's operations. The Mayor serves as the chief executive officer and the Comptroller serves as the chief fiscal officer of the City. The City provides a variety of services to its residents including police and fire protection, sewer utilities, and parks and recreation programs.

The City Comptroller and his staff are responsible for overseeing and managing the City's financial operations, including maintaining the accounting records, collecting real property taxes and other revenues, investing City funds, processing payroll, disbursing funds and preparing required financial reports.

The City's operating expenditures are funded primarily with revenues from real property taxes, sales taxes, sewer receipts, and State and Federal aid. For the 2009 fiscal year, the City budgeted expenditures that totaled \$62.5 million for the general fund.

Objective

The objective of our audit was to determine if the City has established effective internal controls over the financial operations of the Comptroller's Office and information technology. Our audit addressed the following related questions:

- Have adequate internal controls been established over the financial operations of the City Comptroller's Office to ensure that City assets are properly safeguarded?
- Are internal controls over the City's information technology (IT) system appropriately designed to protect electronic data?

Scope and Methodology

We examined the internal controls over payroll, cash receipts, and cash disbursements in the City Comptroller's Office and IT, and reviewed selected financial transactions, records, and reports for the period April 1, 2007 to January 31, 2009.

Our audit disclosed areas in need of improvement concerning information technology controls. Because of the sensitivity of this information, certain vulnerabilities relating to passwords are not discussed in this report but have been communicated to City officials so they could take corrective action.

**Comments of
Local Officials and
Corrective Action**

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.

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials disagreed with certain aspects of our findings and recommendations in our report, but indicated that they planned to implement some of our recommendations. Appendix B includes our comments on the issues raised in the City's response letter.

The Common Council 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 Common Council to make this plan available for public review in the City Clerk's office.

Comptroller's Office

The Comptroller is responsible for designing internal controls for his Office that help safeguard the City's resources and ensure that these resources are used economically and efficiently. An adequate system of internal controls includes clear policies and procedures that promote effective operations, the prudent use of resources and the adherence to applicable laws and regulations. Further, an effective system of internal controls provides for the segregation of duties such that no single individual controls all phases of a transaction. When it is not practical to segregate duties because of limited staff resources, City officials should establish compensating controls. Such compensating controls could require other administrative employees to periodically review the work of the staff under their direction, and for the periodic rotation of work duties.

The Comptroller has not adopted comprehensive policies and procedures to provide guidance and internal controls for payroll processing, claims processing, wire transfers and cash receipts. This lack of guidance, in the form of written policies and procedures, has resulted in a lack of segregation of duties and a lack of compensating controls over certain aspects of the City's financial operations. As a result, there is an increased risk that errors and irregularities will occur and not be detected.

Payroll Processing

Written payroll policies and procedures, combined with job descriptions affixing responsibilities for specific payroll activities, help to ensure that employees understand their role in the payroll process. An important principle of internal control requires that no individuals have uncontrolled access to an entire processing cycle. Management should not allow one individual to perform the three key payroll duties of authorization (i.e., entering employee records and making changes in hourly and annual salary rates in the payroll software), recordkeeping, and asset custody (i.e., signing or distributing checks). For the 2007-08 fiscal year, the Comptroller's Office processed approximately \$30 million in payroll expenditures.

The Comptroller has not adopted comprehensive written policies and procedures to provide guidance and internal controls over payroll processing and he did not ensure that payroll duties were adequately segregated. A timekeeper and two payroll clerks on the Comptroller's Office staff are responsible for processing the City's payrolls. The timekeeper is responsible for adding new employees to the payroll system, inputting payroll changes, and processing payroll for salaried employees. She also sorts the signed pay checks for distribution to

the departments. The two payroll clerks are responsible for entering the hours worked by hourly employees, printing signed pay checks and maintaining the leave records. One of these clerks serves as a back-up for the timekeeper when she is absent. All three of these employees have full access to the computerized payroll records and are able to make changes to salaries, pay rates or hours worked, and their duties are performed with only minimal oversight. While payroll change forms signed by a department head and/or the Human Resources Department were used to authorize changes to the payroll system (i.e. adding employees to the payroll, updating salary information), there was no review of changes made by the timekeeper and payroll clerks to verify that only authorized changes were made. No other City official or employee tests (spot checks) the accuracy of payrolls and leave accrual records. However, the City did implement an independent review of final payrolls by requiring the Civil Service Department and department heads to certify the payroll registers.

While complete segregation of duties may not be possible, ideally, the human resource functions (adding staff, inputting and updating salary information and maintaining personnel files) should be segregated from the payroll processing duties. Our examination of the City's computerized financial system indicated that the system is able to generate audit logs that show all changes that are made to the payroll application, which user made the change, and the time of the change. These reports could provide a useful tool for management to oversee the payroll process; however, supervisory personnel do not generate or review the available reports. The lack of segregation of duties over payroll without adequate management oversight, including the review of change reports, puts the City at risk for unauthorized payroll transactions.

We tested 30 changes that were made to the payroll application during our audit period (including salary changes and employees added and deactivated in the system) to ensure the changes were supported by an approved employee payroll change form. Our testing disclosed that all the changes were authorized. We also tested the accuracy of 20 employees' gross pay totaling about \$913,000 during the 2007-08 fiscal year¹ and found that eight of the 20 employees did not receive the correct gross pay, resulting in overpayments and underpayments to these employees totaling \$5,702 and \$604, respectively. For example,

¹ The police and fire departments enter the time worked for their employees into separate computer systems and the data is automatically transferred to the payroll system in the Comptroller's Office. Since the objective of this audit focused on the internal controls in the Comptroller's Office, we did not include Police and Fire Department employees in our audit sample.

we noted that one employee was compensated for working 306 hours from September 10, 2007 through November 7, 2007, although she was not working and had used all of her accumulated leave time, resulting in an overpayment of \$5,401.

A payroll clerk informed us that the overpayment occurred because the employee's department head did not submit a payroll change form to notify the Payroll Department that the employee was on unpaid leave. Additionally, the Payroll Department did not receive a summary timesheet from the employee's department for three payroll periods while the employee was on unpaid leave, yet continued to process the payroll and compensate the employee as if she were working.² Salaried employees are paid on the last day of the pay period (Friday) for the work performed through that day. The Comptroller's Office does not receive salaried employees' summary timesheets until the Monday following the pay date. The Payroll Department would normally dock employee pay in the next payroll cycle if an employee did not work the required hours and did not have sufficient leave accruals available to cover the absence.³ However, in this case, the Payroll Department did not ensure that it received the summary timesheets and it continued to pay her for working her regular hours even though she was absent.

Upon the employee's return to full-time employment at the City, the error was discovered and an agreement was entered into where \$150 would be garnished from each of the employee's subsequent biweekly paychecks in order to repay the City for the overpayment. As a result, the employee had \$3,600 garnished from her wages during the period November 21, 2007 through November 7, 2008.⁴ However, the City never recouped the total remaining unpaid balance of \$1,801 because the City eliminated the employee's position effective October 8, 2008 and it failed to collect the remaining balance from her final checks.

The other seven employees did not receive the correct gross pay during the 2007-08 fiscal year for various reasons. For example, there were several clerical errors by the Payroll Department employees in calculating the total number of extra and overtime hours worked by employees. We also noted a \$100 payment to an employee for a

² In addition to the employee included in our sample test, two other employees are reported on the summary timesheet for this department. The Comptroller's Office continued to process the pay checks for all three employees for three pay periods without receiving the summary timesheets.

³ Salaried employees who work extra hours or earn overtime during a pay period are compensated for the extra/overtime hours in the next payroll cycle.

⁴ We expanded our payroll testing for this employee into the 2008-09 fiscal year to determine if the City fully recovered the overpayment.

clothing allowance to which he was not entitled based on his collective bargaining agreement. Additionally, we noted that four salaried employees were compensated at their higher 2007-08 fiscal year hourly rates for the extra and overtime hours worked during the last biweekly payroll of the previous fiscal year when their hourly rates were lower. Since timesheets for salaried employees are received after the pay date, the overtime was paid in the subsequent pay period. The Payroll Department employees did not take into consideration the time when the extra and overtime hours were actually worked by the employees when processing the payroll.

A good system of accounting for employee leave time (vacation, sick, etc.) includes periodically verifying that the records for leave time earned and used, and leave allowances to which employees are entitled, are accurate and prepared timely. In certain instances, unused leave days can be converted to cash payments which represent a considerable monetary benefit for employees. The Comptroller's Office had no system in place for someone other than the payroll clerks who maintain the leave accrual records to spot-check the accuracy of postings to records and to review the available balances. Failure to accurately record and account for leave accruals may result in overstated leave balances, which eventually may be converted into cash payments that exceed the amount the City is required to pay. As part of our audit, we reviewed a sample of 20 employees' leave accrual records for the 2007-08 fiscal year to ensure that leave was earned in accordance with collective bargaining agreements or the City's employee handbook, and to verify that the leave usage recorded in time records submitted to the Comptroller's Office was properly deducted from the employees' leave records. We found that the Comptroller's Office was not effective in ensuring that leave balances were accurate. For example:

- Four employees' compensatory leave balances exceeded the 30-day maximum accumulation established by their collective bargaining agreements, as of the fiscal year ending March 31, 2008. The four employees had a combined total of 129.75 hours in excess of the amount allowed, valued at \$3,253.
- We identified eight instances totaling 36.5 hours (\$886) when an employee used leave time, but the leave time was not deducted from the employee's leave accrual records.
- Leave time was improperly added to employees' leave accrual records in three instances totaling 50.5 hours (\$681). One of the three times an employee was credited with 40.5 hours of compensatory leave for overtime hours worked during a pay period, even though the employee received overtime pay for those hours.

- Leave time was improperly deducted from employees' leave accrual records, in five cases totaling 32.5 hours (\$837). One of the five instances resulted because an employee was charged a full day of compensatory leave and sick leave for the same day of absence.
- Employees were not credited with the proper amount of compensatory leave time earned in four instances totaling 23 hours (\$361).

Accurate leave records are essential in determining the proper amount of termination payments that are due to employees who retire or resign from their positions and ensuring that City employees are compensated for the correct amounts to which they are contractually entitled. The number of errors identified during our testing indicates that the payroll processing system needs substantial improvement. Although the cost to the City resulting from the exceptions disclosed by our testing was not substantial, the cumulative impact of such errors and irregularities over time could result in a material liability.

Claims Processing

Internal controls over the payment of claims are intended to ensure that every claim has enough supporting documentation to determine that it complies with City policies and that the amounts paid represent actual and necessary City expenses. When internal controls are not designed appropriately or operating effectively, it increases the risk that errors and irregularities may occur and not be detected and corrected. Key elements of a system that accomplishes these internal control objectives are the provision of a careful, independent review of claim documentation prior to payment and the proper segregation of key approval, processing, and cash disbursement duties so that no single individual controls all phases of the claim payment process. If duties cannot be ideally segregated, management must provide increased supervisory review to mitigate risks.

The Comptroller did not adopt comprehensive written policies and procedures to guide the audit and payment of claims by the staff in his Office. The internal controls over claims processing do not provide an independent claims audit function, nor do they provide for the adequate segregation of duties. Two individuals in the Comptroller's Office are responsible for the entire claims payment function, including processing, approving and paying claims. A senior account clerk/typist is responsible for matching purchase orders for goods with the related invoices, reviewing and approving the claim packets, inputting the payments into the computer system, printing signed checks and sending the checks to the vendors. A disbursement officer is responsible for reviewing and approving vouchers and invoices for

services received by the City. Although the senior account clerk/typist generally enters the payments for services into the computer system and prints the related checks, the disbursement officer performs all of these functions when the senior account clerk/typist is absent. Both of these employees are able to add new vendors to the computer system and update vendor names and contact information within the system. These duties allow these employees to control all phases of the cash disbursements process, which could result in inappropriate disbursements being initiated, processed and concealed.

We also found a weakness in controls over the Comptroller's signature card that is used to sign checks. The signature card is stored in a lock box in the Comptroller's office. The key to the lock box is kept by the box and accounts payable staff are able to obtain access to the signature card and the blank check stock when they need to print checks.⁵ Staff members are required to sign a log when they use the signature card. They must include the date; their name; the time they signed the card out and back in; and the reason for using the card (ex. accounts payable checks or payroll checks); but they do not record the check numbers they are using.

Although the sign out sheet provides a limited degree of accountability, it would not prevent accounts payable staff from processing an inappropriate check because the blank check stock paper is not pre-numbered and staff members are able to assign the beginning check number for the series of checks to be printed.⁶ As a result, there is no accountability for check number sequences and no independent verification that all checks are proper. Furthermore, the City does not receive cancelled checks or check images back from the bank and there is no process in place for someone independent of the cash disbursements function to periodically review check images available on-line with the bank. Given the weak controls over the check signing process, such a review of cancelled checks would not only serve as a deterrent against fraud, but it would enable staff in the Comptroller's Office to identify possible improprieties in a timely manner. However, the better course of action would be to segregate duties so staff responsible for processing accounts payable cannot also approve the payments or sign and distribute the related checks.

⁵ Payroll clerks also have access to the Comptroller's signature card to print payroll checks.

⁶ Checks are printed using software that prints all the necessary information on blank check stock (paper with only the color background of the check on it). This information printed includes the City's name, bank name and account number, payee, check number, amount, date, and the Comptroller's facsimile signature.

The Comptroller informed us that he provides oversight by reviewing purchase orders before they are sent to vendors and reviewing computerized check registers provided by the individuals who process the accounts payable. However, the Comptroller has no assurance that all checks are included on the check registers he is given and his review of purchase orders, while beneficial, is not a substitute for the independent audit and approval of the final claim packets.

The Comptroller's failure to design and enforce strong controls over the approval and payment of claims raises concerns about the risk that improper or erroneous payments might occur and not be detected. To address this risk, we selected 40 payments totaling about \$2.38 million and examined the claims, supporting documentation and the associated cancelled check. We found four payments totaling approximately \$100,400 that did not contain adequate supporting documentation. Three of the claims totaling \$90,000 were payments related to grants or loans administered by the Department of Urban and Economic Development. These claims did not contain the supporting loan or grant agreements, but City officials provided the agreements upon our request. One claim for legal services totaling \$10,400 was not supported by detailed invoices.

When claims are paid without adequate supporting documentation and independent approval, there is an increased risk that improper payments will be made. While our testing did not reveal any fraudulent cash disbursements, this does not diminish the need for the Comptroller to either segregate the claims processing, audit and payment duties or to implement compensating controls.

Wire Transfers

Proper segregation of duties is an important control over the electronic transfer of funds (wire transfers). Without proper segregation of duties, one person could be in a position to initiate an inappropriate transaction and conceal it. At least two individuals should be involved in each electronic transaction. The authorization and transmitting functions should be segregated and, if possible, the recording function should also be delegated to someone who does not have either approval or transmitting duties.

The Comptroller has not designed adequate internal controls over wire transfers. There are no documented policies or procedures to identify the process to be used for authorizing, initiating, documenting, reconciling or monitoring wire transfers. The principal accounting supervisor performs and records internal and external wire transfers with little oversight. He executes transfers without the approval of another individual, and the banks do not provide written confirmation or callbacks to another official or employee for transfers made to non-City accounts. To help mitigate these control weaknesses, an

employee independent of the wire transfer process is responsible for reconciling the City's bank accounts. While reconciliations by an independent employee would help to detect an inappropriate transfer that had already been made, this control would not necessarily prevent an improper transaction from being executed.

We tested 132 wire transfers recorded on the City's bank statements totaling about \$34.2 million for October 2008. We found all transfers during the month were between City bank and investment accounts or to an entity entitled to the funds (ex. payments for Federal and State taxes, debt service, health and dental insurance, and the State retirement system.) Although our testing disclosed no exceptions, when City officials do not exercise supervisory review over wire transfers, this lack of monitoring may lead to incorrect or inappropriate transactions.

Real Property Tax Penalties

Pursuant to the City Charter, the City charges a 2 percent penalty on real property taxes received within five days of the due date (April 30th). After that date, the City charges a 5 percent penalty for the first month and an additional 1 percent penalty each month thereafter until the tax is paid. The cashiers in the Comptroller's Office have the ability to change the effective date of the tax receipts in the financial system. This enables them to back date receipts in the records to avoid recording a penalty for payments received after the penalty free period. Cashiers are not required to obtain supervisory approval prior to changing the cash receipt dates.

We reviewed recorded tax payments that were entered in the computer system from May 6 to May 9, 2008. Out of 250 payments totaling \$163,400, 107 payments totaling about \$60,700 were back-dated to reflect an April 30, 2008 receipt date and no late fees were recorded. The late fees for these payments would have been about \$3,000. City officials cannot determine whether the receipts were entered into the computer on the day they were received or if the cashiers did not post the records timely. The cashiers did not document any reason for changing the effective date for these receipts. According to one cashier, when tax payments are received through the mail, they will enter receipts in the system using the postmark date on the envelope so the system does not assess a penalty for payments mailed during the penalty free period but received afterwards.

Accountability is weakened when cashiers are able to post date receipts to avoid collecting or recording tax penalties without supervisory approval. The approval and justification for the forgiveness of penalties should be documented.

Interdepartmental Cash Receipts

Various departments collect moneys and remit the funds to the Comptroller's Office for deposit and recording in the central accounting records. The City Charter requires the Comptroller to prescribe the time and manner in which moneys received by the departments shall be reported and paid to the Comptroller's Office. It also requires the Comptroller to prescribe and control systems for the issuance of serially press-numbered receipts to be used by all City departments. The use of consecutively press-numbered receipts helps to verify the amounts of money collected by each person responsible for collecting cash. In order for the issuance of receipts to be a meaningful and strong control, receipt books must be inventoried, safeguarded and accounted for by someone independent of the collection process. In addition, each City officer and employee who collects fees should be held accountable for all unused receipts and receipt books issued to him/her and there should be a clear audit trail from completed receipts to remittances to the Comptroller's Office.

The Comptroller has not provided written guidance to departments on the time and manner in which moneys should be reported and remitted to the Comptroller's Office. Additionally, the Comptroller has not established a control system for departments to issue serially press numbered receipts. We tested 50 remittances from various departments to the Comptroller's Office totaling \$73,287.⁷ Each department has its own procedures for recording collections and reporting and remitting funds to the Comptroller's Office. Most departments provide some record of accountability such as a summary cash sheet when they remit funds to the Comptroller's Office; however, we noted that some departments did not submit any documentation with funds remitted and one department submitted incomplete documentation.

For example, the Youth Bureau and Public Safety Department remitted funds to the Comptroller's Office without submitting a report or listing of the revenues and fees collected. When departments do not submit a report or other documentation with remittances to the Comptroller's Office, there is nothing for the Comptroller's Office staff to compare to the cash and checks remitted. Such documentation provides a level of assurance that all funds have been accounted for and helps create an audit trail between departmental records and the records in the Comptroller's Office. For those departments that did not submit a report of cash receipts to the Comptroller's Office, we reviewed the departmental records to try to verify that the receipts recorded by the Comptroller's Office agreed with what the departmental records

⁷ Our testing included remittances from the Parking Violations Bureau, Youth Bureau, City Clerk, Assessors Office, Golf Course, and the Departments of Civil Service, Codes Enforcement, Vital Records, Public Safety, and Employee Benefits.

show was remitted. We were unable to confirm remittances by the Code Enforcement and Public Safety Departments of \$234 and \$154.50, respectively, because the departments did not have receipts or other supporting documentation for the moneys collected and remitted to the Comptroller. In addition, we were unable to confirm four remittances from the Youth Bureau totaling \$1,360, because the department sometimes completed two separate receipts for the same cash collection.⁸ As a result, City officials could not determine with any certainty the amount of money that was actually collected and remitted to the Comptroller's Office. While the golf course provided receipts along with the moneys it remitted to the Comptroller's Office on three occasions, it paid a total of \$408 more to the Comptroller's Office than the receipts showed. Further, while staff members in the Comptroller's Office complete press numbered receipts for moneys received by departments, a receipt copy is not always given to the person who remits the funds. As a result, the departments do not always receive confirmation from the Comptroller's Office when they remit money.

Our testing disclosed that moneys were recorded and deposited in the bank by the Comptroller's Office in a timely manner. However, the Comptroller could strengthen controls and improve accountability by establishing procedures concerning the use of serially, press-numbered receipts by departments that receive moneys and establishing reporting and remittance requirements for when the money is turned over to the Comptroller's Office. Departments should ensure they obtain a receipt from the Comptroller's Office to document the transfer of funds.

Recommendations

1. The Comptroller should establish written procedures that clearly define roles and responsibilities to guide his staff in the performance of their day-to-day duties.
2. The Comptroller should segregate payroll related duties to the extent possible or establish additional supervisory review procedures to mitigate the risk of payroll errors or irregularities.
3. The Comptroller should ensure that supervisory personnel or someone independent of the payroll process periodically reviews change reports generated from the payroll system.
4. The Council should take the appropriate steps to recover the remaining unpaid balance from the employee that was overpaid when her leave balances were depleted.

⁸ Receipts issued by the Youth Bureau were not press numbered.

5. The Comptroller should establish procedures to ensure that all timesheets are received and reviewed to verify payroll accuracy.
6. The Comptroller should assign an individual, other than the employees responsible for updating and maintaining leave accrual records, to spot-check the accuracy of postings to leave accrual records and leave accrual balances.
7. The Comptroller should ensure that employee fringe benefits coincide with the terms of applicable collective bargaining agreements or the City's employee handbook.
8. The Comptroller should ensure that the individual(s) responsible for auditing and approving claims are independent of the recordkeeping and check signing/distribution functions. Where incompatible duties cannot be appropriately segregated, the Comptroller should establish effective supervisory review procedures to mitigate risks.
9. The Comptroller should ensure that all claims include adequate support for the expenditure prior to payment.
10. The Comptroller should segregate cash transfer duties to the extent possible and establish procedures for transfer authorizations and written confirmations and/or callbacks from the bank to an individual who does not initiate wire transfers.
11. The Comptroller should develop procedures to monitor and control the ability of cashiers to change the effective date of tax receipts to avoid recording late penalty fees.
12. The Comptroller should provide written guidance to departments on the time and manner in which moneys should be reported and remitted to the Comptroller's Office. Departments should obtain a receipt from the Comptroller's Office when moneys are remitted.
13. The Comptroller should establish a control system for departments to issue serially press numbered receipts.

Information Technology

An effective system of internal controls to safeguard computerized data includes policies and procedures adopted by the Council to minimize the loss or corruption of essential data. Computer data is a valuable City resource. The City relies on computer data for making financial decisions and for reporting to State and Federal agencies. If the computers on which this data is stored fail or the data is lost or altered either intentionally or unintentionally, the results could range from inconvenient to catastrophic. Even small disruptions in electronic data systems can require extensive effort to evaluate and repair. For this reason, access to computer data systems must be controlled and monitored to reduce the risk of misuse and/or alteration of data resulting in potential financial loss to the City. A formal disaster recovery plan is necessary to provide guidance on the prevention of the loss of computer data as well as the recovery of computer data in the event of a disaster. We found that the Council has not established internal control policies and procedures to effectively address the safeguarding of computer data.

Server Room Security

An effective internal control system restricts physical access to IT system components such as servers, switches and wiring closets. Unrestricted access to the servers endangers the security of the City's computer system. An individual could damage or destroy costly equipment that would require considerable staff time and money to replace or repair the equipment.

City officials have not established policies or procedures to ensure that system equipment is located in a secure location. We inspected the City's IT equipment and found that the network servers and components are located in an unsecured office that is accessible to the City Comptroller's staff. Access to the room was not monitored or controlled; any City employee who worked in the proximity of the room could easily gain access. Under current conditions, it would be difficult for City officials to prevent unauthorized or malicious access to network equipment or to identify the party responsible if such access did occur.

Security enhancements can help protect City IT system components from damage and loss. Access to IT system components must be restricted and controlled through safeguards such as physically securing network components in a locked room with adequate ventilation where access is controlled and tracked. Without physical security, all other security measures may be ineffective. Physical threats, whether internal or external, malicious or inadvertent, could

lead to damaged or stolen hardware and/or the release of personal or other confidential information. These security breaches can result in monetary loss and significant effort to correct, and could possibly lead to costly litigation for the City.

User Access

A component of good internal controls over computer data is policies and procedures designed to limit access to data. The City should restrict access to authorized users, based on the needs of their particular job functions. User accounts identify users and establish relationships between a user and a network, computer, or application. These accounts are created by the system administrator and contain information about the users, such as access rights to files, applications, directories and other computer resources. A good system of controls requires users to enter their user name and authentication to access a network, computer, or application. The computer compares this information with its database of user accounts and, if a match is found, gives the user access to those resources stipulated in his/her user account. City policies should require written documentation for the addition, deletion or change in access rights in order to provide an effective audit trail.

The City does not have policies and procedures that address the assignment of user access, specifically the authorization and documentation of the addition, deletion or change of a user account. During our review of access rights, we found that the City's IT consultant adds, changes and deletes employee access rights based on verbal directive from Department heads or supervisors. Without appropriate documentation, City personnel are unable to determine who authorized access, when access was given or revoked, and what access was permitted.

Additionally, we found that the City has not limited users' access to only the computer functions necessary to fulfill their job responsibilities. For example, we determined that the timekeeper, two payroll clerks, and the principal accounting supervisor have "all access" to the software application that is used to process payroll, and thus have the ability to enter and delete employees and change hourly and annual salary rates. This level of user access has been granted to all four employees even though only the timekeeper has been designated the responsibility for making changes to the payroll application, with one of the payroll clerks serving as backup in her absence. We also determined that two individuals in the Comptroller's Office, in addition to the two payroll clerks, have "all access" to the software application that is used to maintain leave accrual records, although only the two payroll clerks' job responsibilities entail maintaining leave accrual records on a day-to-day basis. With this

level of access, these individuals have the ability to enter, delete, or modify leave accrual transactions, which creates the opportunity for the manipulation and concealment of transactions.

Data Backup

It is important for City officials to back up (i.e., create a copy) computer processed data on a routine basis and the copy must be stored at an environmentally and physically secure offsite location for retrieval in case of an emergency. The backup data needs to be periodically tested to ensure that the data could actually be restored in the event of a problem with the server.

Although the City performs daily and weekly data backups of its financial systems, it does not store the data backup tapes in a secure off-site location. Instead, the data backup tapes are kept in the same room as the server. Storing backup tapes at the same location as the server subjects the tapes to many of the same risks (disasters) as the original data and defeats the purpose of the backup control process. In addition to the City's daily and weekly back-up procedures, the City's IT consultant informed us that he copies the data to a portable hard drive every few days and takes it home with him. However, he does not perform a complete system back-up so the City would not be able to use this backup to restore operations in the event of a disaster. Further, the IT consultant could be exposing the City's sensitive and confidential data to an increased risk of loss or theft by taking the backup copies home.

Also, we noted that the City does not have a formal process in place to periodically test whether it could restore system data from the backups. Therefore, it has no assurance that backup tapes will work and the City risks losing computer-processed data if the system were to become compromised and backup files were not able to restore it to normal operations.

Disaster Recovery

A system of strong internal controls also includes a disaster recovery plan that describes how an organization might deal with potential disasters. A disaster could be any sudden, unplanned catastrophic event that compromises the integrity and the data of the IT systems; this could include fire, flood, a computer virus, vandalism, or inadvertent employee action. Contingency planning to prevent loss of computer equipment and data as well as the procedures for recovery in the event of an actual loss is crucial to an organization. The plan needs to address the roles of key individuals and include precautions to be taken to minimize the effects of a disaster so City officials will be able either to maintain or quickly resume day-to-day operations. The plan should also include significant focus on disaster prevention.

City officials have not developed a comprehensive disaster recovery plan. Consequently, in the event of a disaster, City personnel have

no guidelines or plan to follow to help minimize or prevent the loss of equipment and data or guidance on how to implement disaster recovery procedures. The lack of a disaster recovery plan could lead to loss of important financial data along with a serious interruption to City operations, such as not being able to process checks to pay vendors or employees.

Recommendations

14. The Council should adopt comprehensive policies and procedures relating to all key aspects of the City's IT operations, including but not limited to physical security, user access, back-up data and disaster recovery.
15. City officials should ensure that access authorizations are documented and access rights are given to individuals based on their job duties.
16. City officials should store backups of City information at an environmentally and physically secure off-site location. In addition, this data should be periodically tested to verify that it is capable of restoring the City's system.

APPENDIX A

RESPONSE FROM CITY OFFICIALS

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



CITY OF UTICA

Office of the Mayor

1 Kennedy Plaza, Utica, New York 13502

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email: mayor@cityofutica.com

David R. Roefaro, Mayor

July 7, 2009

[REDACTED]
[REDACTED]
Office of the State Comptroller
State Office Building, Room 409
333 E. Washington Street
Syracuse, NY 13202-1428

Dear [REDACTED],

Enclosed you will find the City of Utica's response to the report entitled "Financial Controls in the City Comptroller's Office and Information Technology."

Sincerely,



David R. Roefaro, Mayor
City of Utica



Michael T. Cerminaro, Comptroller
City of Utica,

Response to:
Financial Controls in the City Comptroller's Office and Information Technology

An audit of the City of Utica was conducted by the Office of the New York State Comptroller for the period of April 1, 2007 through January 31, 2009. A report entitled "Financial Controls in the City Comptroller's Office and Information Technology" was issued as a result of that examination. This is the City of Utica's response to that report.

Audit Results

The report states: "The Comptroller has not adopted comprehensive written policies and procedures to provide guidance and internal controls for payroll"

While we agree that the City Comptroller's office never has had formal written documentation for various departmental policies and procedures, this does not mean that there are no "policies and procedures" in place. These long established and understood policies and procedures are essential to the operations of the office. In fact, through the years, countless numbers of errors have been caught and corrected because of the due diligence of our office personnel following long established policies and procedures.

Payroll Processing

The report states "All three of these employees have full access to the computerized payroll records and are able to make changes to salaries, pay rates or hours worked, and their duties are performed with minimal oversight." While it is true that the employees who process the bi-weekly payroll can make the changes listed above, it is not true that those duties are performed with minimal oversight. Each individual payroll is subject to review by the Comptroller, Deputy Comptroller and Principal Accounting Supervisor during any and all stages of processing. The City Comptroller then authorizes the printing of the payroll checks.

See
Note 1
Page 28

Payroll registers are then issued to all departments prior to the release of paychecks. Department heads then review the information on the payroll registers to ensure accuracy. For those departments with hourly employees, the department head checks to make sure that the number of hours submitted to the Payroll Department corresponds to the number of hours on the payroll register. Further, department heads check to ensure that the appropriate changes have been made for salaried employees since he or she initiates those changes by submitting a payroll change sheet. After the department head signs the payroll register, it is then forwarded to the Utica Municipal Civil Service Commission. The commission staff reviews the payroll registers to ensure that titles conform to Civil Service law and that salaries are in accordance with collective bargaining agreements. If those two conditions are met, the payroll register is then certified by the Civil Service Commission. The certified payroll register must be received by the Payroll Department before payroll checks are released.

Also cited in the report are various payroll and other transactions that were said to be erroneous. Upon further investigation, we feel that many of these transactions can be fully accounted for, and that our calculations are correct.

See
Note 2
Page 28

Claims Processing

The report states that "The internal controls over claims processing do not provide an independent claim audit function, nor do they provide for the adequate segregation of duties."

One of the internal controls not mentioned in the report is the concept of “Positive Pay.” Positive pay is one of the most basic fraud prevention methods in use today. With positive pay, data files are transmitted to the bank, in this case, by the Principal Accounting Supervisor, detailing all check numbers, amounts and payees for all checks issued by the city. If a check is presented to the bank with information that differs from any of the information previously provided, the Principal Accounting Supervisor is contacted to make a decision as to whether the check is to be paid or returned. Positive pay is used to prevent external as well as internal fraud and was implemented shortly after the current City Comptroller took office. Positive pay is in use for both the payroll and accounts payable bank accounts.

See
Note 3
Page 28

Regarding the segregation of duties in the Claims Processing function of the Comptroller’s Office, it is sometimes necessary for one person to process a claim and produce a check. The city’s Accounts Payable function cannot come to a halt due to one individual’s vacation, sickness or absence. Because two individuals work in Accounts Payable, it is not only proper, but necessary, that both individuals be able to produce checks in the absence of the other. However, a check is produced only after notification and authorization by the City Comptroller.

We feel that adequate steps have been taken to mitigate the risk of fraudulent disbursements. All claims are reviewed by the Comptroller and the check register is signed by the Comptroller prior to payment and that, as well as other steps taken led to the examiners not finding “any fraudulent cash disbursements.”

See
Note 4
Page 28

Wire Transfers

The report states that “The principal accounting supervisor performs and records internal and external wire transfers with little oversight.” We do not feel that these transfers are done with little oversight. The Deputy Comptroller has access to the banking software used to initiate these transfers and can view them at any time. Further, the Deputy Comptroller can view wire transfers done in the past for any given period of time.

See
Note 5
Page 28

At the end of any given month, the bank reconciliation process begins. All of the city’s bank accounts are reconciled to the city’s general ledger. This reconciliation process is done by the city’s Senior Auditor and is independent of the individual making wire transfers. As part of the bank reconciliation process, all wire transfers are reviewed. Any suspicious transfers would then be brought to the attention of the Comptroller.

See
Note 6
Page 28

The fact that 132 wire transfers totaling \$34.2 million were tested, and “all transfers during the month were between City bank and investment accounts or to an entity entitled to the funds (ex. payments for Federal and State taxes, debt service, health and dental insurance, and the State retirement system.)” and “testing disclosed no exceptions” are testament to the internal controls already in place.

Real Property Tax Penalties

The report states “With respect to cash receipts, we found that cashiers in the Comptroller’s Office have the ability to change the effective date of the tax receipts in the financial system to avoid recording a penalty for payments received after the penalty free period.” The report concludes that 107 payments processed from May 6 through May 9, 2008 were back-dated to reflect an April 30, 2008 receipt date and further, “the late fees for the payments would have been about \$3,000.”

In accordance with the tax collection rules set forth by the State of New York, any tax payment which has a postmark showing that the payment was mailed on or before the due date of that tax, must be treated by the tax collector as an on-time payment.

During the month of April of any year, it is typical to process over thousands of tax payments. The final date to pay before a late fee is assessed is April 30. Many of the tax payments that are made over the counter occur during the last week in April. Likewise, many of the tax payments received by mail are postmarked in the last

few days in April. It is not unusual for the cashiers to be processing on time tax payments five to seven business days after the due date. It is not only proper, but necessary to change the effective date of the payment. Further, it is our contention that that the late fees on these payments should be zero, as they were on time payments.

Interdepartmental Cash Receipts

The report states that “the Comptroller has not provided written guidance to departments on the time and manner in which moneys should be reported and remitted to the Comptroller’s Office.”

The City’s Comptroller’s office has worked with the various departments that collect money to ensure the accuracy of monies collected and remitted to the Comptroller’s Office. We realize that not all money collected by the city can be paid directly to the Comptroller’s Office. For example, individuals wanting to play golf at the city-owned golf course cannot be expected to come to City Hall to pay to do so. A similar situation exists with the Youth Bureau, which runs programs throughout the city and whose offices are not located in City Hall. The Comptroller’s Office will continue to work with those two departments to improve accuracy. It is, however, the goal of the City Comptroller to make the Comptroller’s Office the centralized location for all monies collected at City Hall.

Information Technology

Server Room Security

The City of Utica is in agreement that it has not completely formalized policies and procedures that ensure the City’s IT system components are located in a secure and controlled location. However, it should be noted that the City’s IT system components are behind a single locked door that does grant controlled access only to the City employees in the Comptroller’s Office.

User Access

The City of Utica does not completely agree with the auditors findings with regard to user access. While the City of Utica has no formal policies and procedures it has begun the implementation of [REDACTED] security model (which is approximately 60% complete in terms of user access). [REDACTED] will require users to authenticate to the network with a username and password that grants access to applications, files and directories. Logon successes and failures are logged as well as unauthorized attempts to data access. In addition, the [REDACTED] requires that complex passwords are used and changed every 95 days.

See
Note 7
Page 29

Data Backup

The City of Utica does not fully agree with the auditors findings with regard to data backup. While the data backups are not stored offsite in a secure/environmentally controlled location, data backups do occur every weekday and are stored in a locked fireproof box in an offsite office on a weekly rotating basis where only two key IT individuals have access.

See
Note 8
Page 29

Disaster Recovery

The City of Utica is in agreement that it has no formal disaster recovery plan.

APPENDIX B

OSC COMMENTS ON THE CITY'S RESPONSE

Note 1

During our audit, no one told us that supervisory personnel in the Comptroller's Office actually performed regular reviews of payrolls as part of the City's control procedures, nor did we find documentation of these reviews. Furthermore, we were told that supervisory personnel do not review payroll change logs that show changes made to salaries and pay rates. Supervisory review of these logs provides an effective means to monitor changes made by the employees who process payroll.

Note 2

The day after our exit discussion with City officials, we provided the Comptroller with a list of our specific payroll exceptions and gave him an opportunity to refute our findings. The Comptroller has not provided us with any additional information or documentation to challenge the exceptions we cited in our report.

Note 3

While Positive Pay is a good control over the bank's payment of City checks it does not address the claims auditing process. Positive Pay ensures a check is cashed for the amount it is written for but there is no protection if the check is written for an inappropriate purpose. An independent audit of claims and the segregation of recordkeeping and check signing functions would help ensure that checks are only written for actual and necessary City expenses.

Note 4

When we discussed the City's procedures for processing claims, the Comptroller informed us that he reviewed purchase orders before they were sent to vendors and he reviewed the computerized check registers. He did not indicate that during our audit period he reviewed each claim and we saw no evidence of such a review.

Note 5

While the Deputy Comptroller has access to the banking software used to initiate transfers and he is able to view transfers done in the past, officials did not indicate during our onsite fieldwork that he routinely reviewed wire transfers to ensure they were proper and we saw no evidence of such a review.

Note 6

Based on the additional information provided by the City, we have modified the report.

Note 7

While the implementation of the software application will help improve certain aspects of the City's access controls over its network, it is still important for the City to develop policies and procedures for how user rights will be added, removed and changed in the system. It is also necessary for the City to review current user access rights to the financial system and to restrict access to what the users need to fulfill their job duties.

Note 8

The City's backup procedures should be spelled out in a written policy and made available to IT staff to help ensure that necessary backup procedures are performed and backup files are safeguarded.

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

Our goal was to determine the adequacy of the financial controls in the City Comptroller's Office. To accomplish this, we performed an initial assessment of the internal controls so that we could design our audit to focus on those areas most at risk. Our initial assessment included evaluations of the following areas: payroll, cash receipts and disbursements, cash management, delinquent tax agreements, and information technology.

During the initial assessment, we interviewed appropriate City officials, performed limited tests of transactions, reviewed pertinent documents such as the City Charter, Council minutes, and financial records and reports. In addition, we obtained information from the computerized financial databases and analyzed it electronically. We further reviewed the City's internal controls and procedures over the computerized financial databases to ensure that the information produced was reliable.

After reviewing the information gathered during our initial assessment, we determined where the weaknesses were and evaluated those weaknesses for the risk of potential fraud, theft, and/or professional misconduct. We then decided upon the reported objectives and scope by selecting those areas most at risk. We selected internal controls over the financial operations of the Comptroller's Office and information technology for further audit testing. We focused our attention on whether adequate internal controls had been established over certain financial functions within the Comptroller's Office, specifically in the areas of payroll processing, claims processing and cash disbursements, wire transfers, and cash receipts. We interviewed officials and employees, reviewed available policies, observed transactions, and examined the following documents and records in an effort to determine if the City has designed adequate internal controls over payroll processing, claims processing, wire transfers and cash receipts in the Comptroller's Office:

- Collective bargaining agreements and individual employment contracts
- City Council meeting minutes
- Employee time sheets for regular and overtime pay
- Payroll registers and employee earnings records
- Leave accrual records
- Claims, cancelled checks and check registers
- Wire transfer logs and bank statements for October 2008
- Batched bank deposits, deposit slips and transaction records for cash receipts.

Within information technology, we reviewed provisions related to computer use in the City's employee handbook. We interviewed the City's independent IT consultant and City staff specifically regarding

passwords, physical access to the system, controls within the financial management software, backups of data, and disaster recovery plans. We physically inspected the location of system equipment, viewed various Comptrollers' Office employees' computer screens, and reviewed payroll change reports.

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

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