



STATE OF NEW YORK
OFFICE OF THE STATE COMPTROLLER

March 21, 2001

Mr. Andrew S. Eristoff
Commissioner
The City of New York
Department of Finance
1 Centre Street
New York, New York 10007

Re: Industrial and Commercial
Incentive Program
Report 2000-N-10

Dear Mr. Eristoff:

Pursuant to the State Comptroller's authority as set forth in Article V, Section 1 of the State Constitution and Article 3 of the General Municipal Law, we audited the award of Industrial and Commercial Incentive Program property tax benefits by the New York City Department of Finance for the period April 1, 1996 through September 13, 2000.

A. Background

The New York City Department of Finance (Department) administers the Industrial and Commercial Incentive Program (ICIP or Program). Created on November 5, 1984 pursuant to Local Law 71, ICIP is intended to stimulate economic development. It accomplishes this by offering property tax exemption and abatement benefits to applicants engaging in projects that meet eligibility requirements and involve new construction or the modernization, rehabilitation, expansion or other improvement of existing industrial and commercial properties. For such projects, the Department issues a Certificate of Eligibility (Certificate). Through a series of reporting requirements, the Department verifies ongoing eligibility of certified projects. According to Title 11, Chapter 2, part 4, of the New York City Administrative Code, and Chapter 14, Subchapter A, Part 3 of Title 19 of the Rules of the City of New York, if the Department determines that a project is not in compliance with applicable statutes and rules, the Department may deny, suspend or revoke benefits.

Benefits are based on the increased value of buildings resulting from the eligible projects. The Department's automated Exemption System calculates tax exemption benefit periods and amounts based on project type and location. Once projects are completed, the Department's Abatement of Real Property System (ABRP) calculates abatements, which are credits against the tax liability for eligible industrial projects. For fiscal year 1998, the latest year for which statistics were available at the time of our audit, ICIP exemptions totaled \$100.3 million for 2,373 projects, as shown in the following table.

Location	Number of Projects	Tax Exemption Amounts
Manhattan	152	\$28,716,602
Bronx	381	\$15,073,031
Staten Island	382	\$11,363,666
Brooklyn	705	\$14,099,553
Queens	753	\$31,050,098
Total	2,373	\$100,302,950

For fiscal year 1999, the latest year for which statistics were available at the time of our audit, ICIP abatement benefits totaled over \$6 million, as shown in the following table.

Location	Number of Projects	Total Abatements
Manhattan	9	\$888,108
Bronx	19	\$786,411
Staten Island	2	\$78,449
Brooklyn	115	\$1,582,661
Queens	67	\$2,682,845
Total	212	\$6,018,474

B. Audit Scope, Objective and Methodology

We audited the award of property tax exemption and abatement benefits by the New York City Department of Finance as part of the Industrial and Commercial Incentive Program for the period April 1, 1996 through September 13, 2000. The objective of our performance audit was to determine whether the projects for which tax exemption and abatement benefits were awarded met eligibility requirements set forth in established laws, rules and administrative procedures. To accomplish our objective we examined Department files to assess documentation required to support Program compliance for one random sample and two judgment samples of certified projects. We also interviewed appropriate Department management and staff; reviewed relevant laws, Department procedures and practices; and visited selected project sites.

As is our practice, we notify agency officials at the outset of each audit that we will be requesting a representation letter in which agency management provides assurances, to the best of their knowledge, concerning the relevance, accuracy and competence of the evidence provided to the auditors during the course of the audit. This representation letter is intended to confirm oral representations made to the auditors and to reduce the likelihood of misunderstandings. In the representation letter, agency officials assert that, to the best of their knowledge, all relevant financial and programmatic records and related data have been provided to the auditors. Agency officials further affirm that either the agency has complied with all laws, rules, and regulations applicable to its operation that would have significant effect on the operating practices being audited, or that any exceptions have been disclosed to the auditors.

However, officials of the New York City Mayor's Office of Operations have informed us that, as a matter of policy, Mayoral agency officials will not provide representation letters in

connection with our audits. As a result, we lack assurances from Department officials that all relevant information was provided to us during the audit. We consider this refusal to provide a representation letter to be a scope limitation on our audit. Therefore, readers of this report should consider the potential effect of this scope limitation on the findings and conclusions represented in this report.

We conducted our audit in accordance with generally accepted government auditing standards. Such standards require that we plan and perform our audit to adequately assess those operations of the Department that are included within the audit scope. Further, these standards require that we understand the Department's internal control structure and compliance with those laws, rules, and regulations that are relevant to the operations that are included in our audit scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in the accounting and operating records and applying such other auditing procedures as we consider necessary in the circumstances. An audit also includes assessing the estimates, judgments and decisions made by management. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

We use a risk-based approach when selecting activities to be audited. We therefore focus our audit efforts on those activities we have identified through preliminary survey as having the greatest probability of needing improvement. Consequently, by design, finite audit resources are used to identify where and how improvements can be made. We devote little audit effort to reviewing operations that may be relatively efficient and effective. This report highlights those areas needing improvement, but does identify certain activities that are functioning properly.

C. Results of Audit

Our audit identified several instances where required items of ICIP documentation for certain projects in our samples were not on file. However, for all but one project in our sample the Department concluded that the collective documentation that was available justified eligibility. We did not dispute the Department's judgment or the exercise of its authority regarding its decision not to deny, suspend or revoke benefits based upon the compliance exceptions we noted. For the one project where we noted a compliance exception, the Department was investigating to determine whether benefits were justified. They added that a current effort is underway to streamline ICIP requirements and amend reporting requirements accordingly. Therefore, some compliance tests that we performed during this audit may not be valid in the future. We recommend that these efforts be completed as expeditiously as possible. In the interim, the Department needs to vigorously monitor and assess the eligibility of projects for benefits.

D. Compliance with Requirements for ICIP Property Tax Benefits

The following paragraphs show the results of our audit tests for compliance with requirements to support the award of property tax benefits. The tests involve three audit samples of certified ICIP projects.

Sample Number 1

The Department's records indicate that 1,097 projects had been awarded Certificates between April 1, 1996 and June 5, 2000. We took a judgmental sample of 50 of these projects. The 50 samples were proportionate to the number of applications that had been issued a Certificate for each borough. The sample consisted of a combination of applications with the highest Minimum Required Expenditure (MRE) and applications with MRE amounts between \$10,000 and \$100,000 from each borough.

Our findings for this sample are as follows:

- For all 50 projects, preliminary applications were filed, as required, before the first building permit was received or, if no building permit was needed, before the commencement of construction work.
- Support was available to establish the commencement of construction work for each of the 50 projects, but 14 projects lacked required written applicant notification of the date of commencement of construction work.
- For 34 of the 50 projects, there was no evidence that a final application had been submitted, as required, within 30 business days after construction began.
- Required interim construction reports were not available for 22 of the 25 projects with construction costs exceeding \$1 million.
- There were 26 projects that were supposed to have applicant-provided proof that 50 percent of minimum required project expenses were made within 30 months of certification. For two of these projects, we found no information that showed the applicant had incurred minimum required expenditures. While documentation was available for 15 projects, we noted that four of these lacked required certification from a certified public accountant when costs exceeded \$1 million. For the remaining nine projects, there were no applicant-provided proof of expenditures, but Department assessors' evaluations were available to support the claim that minimum required expenditures had been incurred.
- For 19 projects, there was no evidence that applicants filed required written notice of the completion of construction and final construction report with the Department.
- There were 21 projects for which required notices of the completion of work were available. For one of these, we were unable to determine the timeliness of notification of completion of work because of missing information. However, for the remaining 20 projects, the notices were not provided within 15 business days as required. The elapsed time ranged from 36 days to over two years.
- For 14 of the 20 projects with notices of the completion of work, applicants did not submit a required final construction report within 60 days of project completion. In these instances,

the lateness of the final reports ranged from 74 days to over two years. For two of the 20 projects, the required final construction report was not filed as of September 13, 2000.

- Department District Assessors are to initially inspect projects within 10 business days of a notice to inspect from Department management. These inspections are intended to establish that no construction work commenced before the date of preliminary application for the Program. However, for 17 projects in our sample, the requirement to inspect within 10 business days was not met. The delays ranged from six to 194 days.

Sample Number 2

A Department printout dated February 8, 2000 listed 4,871 ICIP projects with a value of over \$159 million. The printout included 3,925 projects identified as having received property tax exemptions for the 2000-2001 year. We took a random sample 50 ICIP projects included on the listing. Of these 50 projects, 31 had property tax exemptions totaling \$7,274,736 and 19 had no exemptions.

Our findings for this sample are as follows:

- In one instance the ICIP applicant did not submit a Certificate of Continuing Use that is required on or before December 5th of each year to demonstrate continuing compliance with Program requirements. The Department was investigating this matter further to determine whether benefits were justified.
- Documentation indicating that the applicant conducted required searches for Environmental Control Board (ECB) violations at the time of ICIP application was not evident in one case. In another case, documentation indicating that the applicant had conducted the required searches for ECB violations and for Department of Buildings violations (DOB) at the time of ICIP application was not evident.
- We noted 11 instances where documentation indicated DOB violations at the time of ICIP application, but the required support for curing these violations was not on file. Our follow up showed that in three of these cases, the projects currently have outstanding DOB violations, including one project with 35 such violations.
- The Department does not monitor for the identification and cure of violations after the initial application filing for ICIP, although applicants are required to remain in compliance with administrative codes throughout the benefit period. We noted 15 instances where projects currently had at least one outstanding DOB violation. (Department officials advised us that they have taken steps to address this problem. Specifically, the certificates of continuing use now require applicants to certify whether there are any adjudicated, uncured violations.)
- In four instances, District Assessors did not return a completed inspection report to the Department. This report confirms the information concerning an ICIP project as reported on the Certificate of Continuing Use by the site owner.

Sample Number 3

We judgmentally sampled two projects that had the highest abatement benefits in each of the five boroughs of New York City. The ten were selected from 212 projects with ICIP abatements in the 1999-2000 year. Our objective was to determine whether support was on file to establish that property tax abatement benefits were, as required, only granted for completed projects. One applicant owned the two Manhattan projects that we sampled. One of these projects accounted for abatements of \$216,138 and the other accounted for abatements of \$446,862 during the 1999-2000 year. However, we found no evidence that this applicant submitted the notices of completion of work and the cost reports required to substantiate the completion of these projects. Instead, the applicant submitted a box of invoices and cancelled checks that ICIP officials reported were sufficient to support the payment of contract services needed to complete both projects. The remaining eight sampled projects complied with the reporting requirements.

E. Other Matters

During the course of our audit we noted the following control weaknesses that need to be corrected to ensure the continued integrity and correct award of ICIP benefits:

- The Exemption System cannot correctly calculate certain complex exemption benefits. In these instances staff must manually calculate benefits and must directly access the System to make it reflect the correct benefits. To increase operating efficiency, to minimize the risk of human error and to protect the integrity of System files, the Exemption System should be enhanced to eliminate the need for manual calculation of benefits.
- The Department does not have written policies, procedures and guidelines for initiating and reviewing manual calculations or for periodically performing an independent review of Exemption System exception reports for processed transactions using an appropriate sampling methodology. As a result, there is increased risk that intentional or unintentional benefit errors will not be detected in a timely manner.
- The Exemption System does not have controls that will prevent further updates by District Assessors once amounts have been determined and authorized by management. In addition, the exception reports that are produced for the Exemption System do not include all the types of changes that can be introduced to the System's database. A report listing all changes to the database by property, dollar value, originating user and time should be available.

Recommendations

1. *Complete efforts to streamline ICIP eligibility requirements as expeditiously as possible.*
2. *Vigorously monitor and assess the eligibility of projects for ICIP benefits.*

3. *Enhance the Exemption System to eliminate the need to perform manual calculations of benefits.*
4. *Enhance Exemption System exception reporting capability to identify all database changes by property, benefit dollar value, originating user and time.*
5. *Establish and adhere to written policies, procedures and guidelines for initiating and reviewing manual calculations and for periodically performing an independent review of Exemption System exception reports.*
6. *Install Exemption System controls that will prevent further updates by District Assessors once amounts have been determined and authorized by management.*

(Department officials generally agree with recommendations number 1, 2, 4, and 5. They indicate that actions have been undertaken or are planned to implement them. Concerning recommendation number 3, Department officials state that the additional automation recommended to eliminate manual benefit calculations would produce only marginal added value and utility since the vast majority of exemption benefits are already automated. Department officials also state that by implementing routine and enhanced exception reporting identified in recommendation number 4 the objectives of recommendation number 6 should also be accomplished.)

Auditors' Comments: We urge the department to continue to assess the benefit of further automating benefit calculations. In addition, future enhancements to add functionality to the system may also afford an opportunity to eliminate manual benefit calculations.

A draft copy of this report was provided to Department officials for review and comment. Their comments have been considered in the preparation of this report and are included as Appendix A. Department of officials generally agree with most of our recommendations.

Within 90 days of the final release of this report, we request that the Commissioner of the New York City Department of Finance report to the State Comptroller, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons therefor.

Major contributors to this report were Dominick Vanacore, Anthony Carbonelli, Christine Chu, Zenaida Bhuiyan, Marie Farrington, Khondaker Haque, and Nancy Varley.

We wish to thank the management and staff of the New York City Department of Finance for the courtesies and cooperation extended to our auditors during this audit.

Very truly yours,

Jerry Barber
Audit Director



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THE CITY OF NEW YORK
DEPARTMENT OF FINANCE

February 23, 2001

Mr. Jerry Barber
Audit Director
Office of the State Comptroller
State of New York
123 William Street
New York, NY 10038

Re: Draft Audit Report on the award of Industrial and Commercial Incentive Program property tax benefits by the New York City Department of Finance for the period April 1, 1996 through June 30, 2000 Report 2000-N-10.

Dear Mr. Barber,

Thank you for the opportunity to review and comment on the above referenced draft report. Our administration of the Industrial and Commercial Incentive Program (ICIP) seeks to ensure *above all* that only eligible projects receive benefits under the program. Your audit affirms the Department's success in carrying out this important objective. With respect to the compliance issues raised in the report, it is my understanding that virtually all of these will be mitigated once the revised rules we have proposed are adopted.

The following are our comments on the report's specific recommendations.

Auditor's Recommendation No. 1 – The Department should complete efforts to streamline ICIP eligibility requirements as expeditiously as possible.

Agency Response – We agree. The revised rules have been submitted to the New York City Law Department for review prior to adoption.

Auditor's Recommendation No. 2 – The Department should vigorously monitor and assess the eligibility of projects for ICIP benefits.

Agency Response – We agree that eligibility must be vigorously monitored. Based on our review of the audit findings and other previously identified matters, we have determined that improvements are warranted in four specific areas, including initial property inspections, construction expenditure reports, code violations and certificates of continuing use (CCUs). To date, we have issued new written guidelines for handling of CCUs. In addition, the CCU form has been amended to better track adjudicated violations. Some of the other changes that we contemplate must await the adoption of the aforementioned revised rules.

Auditor's Recommendation No. 3 – The Department should enhance the Exemption System to eliminate the need to perform manual calculations of benefits.

ANDREW S. ERISTOFF • COMMISSIONER • DEPARTMENT OF FINANCE
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Agency Response – We’re not sure we agree with this idea. It works in theory, but the vast majority of the exemption benefits are already automated and it is the opinion of our Management Information Systems Division staff that additional automation would produce only marginal added value and utility.

Auditor’s Recommendation No. 4 – The Department should enhance Exemption System exception reporting capability to identify all database changes by property, benefit dollar value, originating user and time.

Agency Response – The exception reports are currently requested on an ad hoc basis. We believe it would be beneficial to produce reports on a set schedule. Once that is completed we will examine the utility and feasibility of enhancing the reports as suggested by the auditors.

Auditor’s Recommendation No. 5 - *Does not appear in report.*

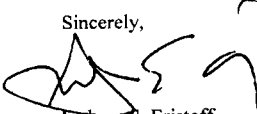
Auditor’s Recommendation No. 6 – The Department should establish and adhere to written policies, procedures and guidelines for initiating and reviewing manual calculations and for periodically performing an independent review of Exemption System exception reports.

Agency Response – Change access is limited to specific members of the exemption staff who have been trained in the appropriate use of the exemption system. However, we agree that written procedures would be useful and they will be developed. We will also initiate independent periodic reviews of the exception reports.

Auditor’s Recommendation No. 7 – The Department should install Exemption System controls that will prevent further updates by District Assessors once amounts have been determined and authorized by management.

Agency Response – As previously mentioned, the exception reports will be produced and scrutinized on a routine basis. We believe that this process will capture any changes that would require updating the exemption system.

That concludes our comments on this draft audit. Thank you again for the opportunity to review and comment on it. If you have any questions or require additional information, please feel free to call me, or Jesse Ostrow at (212) 669-4480.

Sincerely,

Andrew S. Eristoff

c: Jesse Ostrow
Glenn Borin
Warren Hyman
Jacqueline Gold
Eileen Reilly
Krish Kapadia

State Comptroller’s Note:

1. The Department’s response to draft report recommendations number 6 and 7 now corresponds to final report recommendations number 5 and 6, respectively.

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Note
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