CITY OF NEW YORK
OFFICE OF THE COMPTROLLER

John C. Liu
COMPTROLLER

FINANCIAL AUDIT

Tina Kim
Deputy Comptroller for Audit

Audit Report on the New York City Industrial Development Agency's Project Financing, Evaluation, and Monitoring Process

FN11-054A

March 19, 2012

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THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

John C. Liu
COMPTROLLER

March 19, 2010

To the Residents of the City of New York:

My office has audited the New York City Industrial Development Agency's (NYCIDA) project financing, evaluation, and monitoring process. We audit City agencies such as NYCIDA as a means of ensuring that they effectively manage the granting of City resources entrusted them and do so in accordance with applicable rules and regulations.

NYCIDA was established in 1974 to promote, retain, and develop an economically sound commerce and industry base to advance job opportunities in the City. NYCIDA assists industrial, commercial, and not-for-profit organizations in accessing long-term, low-cost financing to acquire or create capital assets. Organizations applying for tax exemption and other City benefits must meet certain economic development criteria, the most important of which is job creation and/or retention in the City. In Fiscal Year 2009, NYCIDA reported a total of 576 projects with total Payments in Lieu of Taxes in the amount of $345.7 million and $497.3 million in tax exemptions, including State and City Sales Tax and Mortgage Recording Tax exemptions.

The audit revealed that NYCIDA generally complied with the Public Authority Accountability Act reporting requirements and filed its Public Authority Reporting Information System report on time. However, our review found several deficiencies in the NYCIDA's review, evaluation, and monitoring of its sponsored projects. Specifically, contrary to NYCIDA's own internal project checklist, NYCIDA did not conduct an independent analysis of the applicant's ability to meet all equity and debt requirements associated with the projects. In addition, our review found no evidence that NYCIDA verified the accuracy of the data submitted in the project application. As a result, NYCIDA could not be assured that certain proposals were viable and able to achieve the employment goals established in their project applications.

We also found that NYCIDA did not follow its own internal procedures to properly monitor project compliance to determine whether companies reported accurate employment data and sales tax exemption benefits and whether the projects were operating as intended. As a result, NYCIDA could not be assured that certain significant projects have fulfilled their promises and were entitled to retain their City benefits.

Further, NYCIDA did not initiate the benefits recapture process and ensure that projects were terminated in a timely manner and according to provisions of the project agreements. As a result, the City did not receive the anticipated return on the benefits it invested in the projects and continued to provide benefits to projects in default. Based on our review of NYCIDA's financial records and related project files, we estimate that of the 42 projects examined at least $16,184,760 in unclaimed recapture benefits involving five companies was lost.

The results of our audit have been discussed with NYCIDA officials and their comments have been considered in preparing this report. Their complete written response is attached to this report.

If you have any questions concerning this report, please e-mail my audit bureau at audit@comptroller.nyc.gov.

Sincerely,

John C. Liu

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Office of the Comptroller
Financial Audit

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AUDIT REPORT IN BRIEF

The New York City Industrial Development Agency (NYCIDA) was established in 1974 to promote, retain, and develop an economically sound commerce and industry base to advance job opportunities in the City and its five boroughs. The organization and powers of NYCIDA are governed by the General Municipal Law (GML) of New York State. Key provisions of the GML allow NYCIDA to establish its own Uniform Tax Exemption Policy (UTEP) guidelines to make project approval or denial decisions. In addition, NYCIDA has the ability to create payments in lieu of taxes (PILOT) and grant Mortgage Recording Tax (MRT) and Sales Tax exemptions.

NYCIDA is managed by a Board of Directors (Board) consisting of 15 members, including representatives from each borough. The president of the New York City Economic Development Corporation (NYCEDC) also serves as the chairman of NYCIDA Board. The GML also provides the Board with the authority to recapture economic benefits or impose sanctions or penalties on projects that are not in compliance. Imposition of the recapture provisions can require the project owner to return all or part of the value of the tax exemption benefits received. NYCIDA contracts with NYCEDC for staffing and administrative services.

NYCIDA is required to comply with certain reporting requirements, including the submission of the Public Authority Reporting Information System (PARIS) report. Industrial Development Agencies are required to file this performance report with the Office of the State Comptroller within 90 days after the close of their Fiscal Year. In its 2009 PARIS submission, NYCIDA reported a total of 576 projects with total PILOT payments in the amount of $345.7 million and $497.3 million in tax exemptions, including State and City Sales Tax and MRT exemptions.

Audit Findings and Conclusions

NYCIDA generally complied with the Public Authority Accountability Act reporting requirements and filed its PARIS report on time. However, our review found several deficiencies in NYCIDA's review, evaluation, and monitoring of its sponsored projects. Specifically, contrary to NYCIDA's own internal Project Checklist, NYCIDA did not conduct independent analysis of the applicant's ability to meet all equity and debt requirements associated with the projects. In addition, our review found no evidence that NYCIDA verified the accuracy of the data submitted in the project applications. As a result, NYCIDA could not be assured that certain proposals were viable and able to achieve the employment goals established in their project applications.

We also found that NYCIDA did not follow its own internal procedures to properly monitor project compliance to determine whether companies reported accurate employment data and Sales Tax exemption benefits and whether the projects were operating as intended. As a result, NYCIDA could not be assured that certain significant projects have fulfilled their promises and were entitled to retain their City benefits.

Further, NYCIDA did not initiate the benefits recapture process and ensure that projects were terminated in a timely manner and according to provisions of the project agreements. As a result, the City did not receive the anticipated return on the benefits it invested in the projects and continued to provide benefits to projects in default. Based on our review of NYCIDA's financial records and related project files, we estimate that at least $16,184,760 in unclaimed recapture benefits involving five companies was lost.

Audit Recommendations

To address these issues, we make seven recommendations, including that NYCIDA:

- Ensure the project financial data received is sufficient and independently verified before a project is submitted for Board approval.
- Perform an independent analysis of the applicant's ability to meet all equity and debt requirements associated with the project and to ensure projects meet the intended purposes, sustain the operations as proposed, and meet the employment expectations to justify all the benefits received.
- Monitor project compliance report submissions to ensure the projects comply with their job retention and creation requirements as established in the application.
- Conduct adequate reviews of project data to ensure Sales Tax exemptions are appropriately claimed and accurately reported.
- Establish internal controls to avoid unauthorized use of Sale Tax Letters.
- Conduct periodic site visits to verify project operations and compliance status.
- Enforce the recapture provisions of the project agreements to ensure City forgone revenue and employment benefits are not lost, and document its decision-making process and the specific criteria used to decide whether or not to enforce the recapture provisions of project agreements.

Agency Response

In their response, NYCIDA officials disagreed with the report's findings and asserted that:

- "Agency Staff and Outside Experts Conduct Significant Financial and Other Due Diligence Prior To Presenting Any Project to the NYCIDA Board of Directors."
- "The Agency Rigorously Monitors all Existing Projects."
- "The Agency Aggressively Pursues its Legal Remedies When Projects Fail to Meet Their Obligations."

Contrary to these assertions, we found that NYCIDA project files lacked required information and adequate project data, which precluded NYCIDA from conducting meaningful analyses of prospective projects. Furthermore, NYCIDA did not adequately monitor project compliance because it failed to ensure that required employment reports, forms, and certificates were submitted. Moreover, even when documentation was submitted, NYCIDA staff did not visit project locations or undertake due diligence testing to verify the accuracy of reported data. As a result, NYCIDA was unaware that a significant number of projects were not compliant with the terms of their agreements. Finally, NYCIDA failed to seek appropriate remedies when projects were in default or otherwise failed to meet their contract obligations. Most notably, nearly $14.4 million was foregone because NYCIDA did not enforce "recapture and termination" provisions in the case of Bear Stearns, one of the entities that defaulted.

NYCIDA also contended that:

> "In addition to its own due diligence, as a conduit issuer, NYCIDA relies on technical expertise provided by underwriters, placement agents, third-party advisors and bond purchasers. . . . The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

NYCIDA's concern that it may be inappropriate to "usurp" the role of consultants, financial advisors, underwriters, placement agents, and borrowers is misplaced. First of all, entities such as these have a vested interest in obtaining City benefits. Furthermore, NYCIDA's reliance on underwriters, placement agents, third-party advisors, and bond purchasers to perform financial analyses fails to provide adequate assurance to safeguard the City's interests in ascertaining the economic viability of prospective projects. Moreover, our audit found that many project analyses were insufficient, unsubstantiated, or unsound. For example, the Bronx Parking Feasibility Study was flawed because projected revenues were based on questionable occupancy rates and inflated attendance figures and did not account for demand fluctuations that would result from price increases and competition. Accordingly, NYCIDA must conduct independent analyses to ensure that City tax benefits are granted only to those companies that will, in fact, create jobs and comply with their financial obligations.

INTRODUCTION

Background

Industrial Development Agencies (IDAs) are not-for-profit public benefit corporations created by special legislation to promote and encourage economic growth, job opportunities, and the general prosperity of a municipality and its inhabitants. The organization and powers of IDAs are governed by the General Municipal Law (GML) of New York State. Among the key provisions of the GML is the requirement for each IDA Board to establish its own Uniform Tax Exemption Policy (UTEP) guidelines to make project approval or denial decisions. IDA-sponsored projects vary depending on the industry needs of the municipalities they serve.

The New York City Industrial Development Agency (NYCIDA) was established in 1974 to promote, retain, and develop an economically sound commerce and industry base to advance job opportunities in the City and its five boroughs. To carry out its mission, the GML provides NYCIDA with the capacity to issue conduit debt on behalf of the City. In addition, NYCIDA has the ability to create payments in lieu of taxes (PILOT), which are real property tax-based exemptions consisting of land tax abatement and building tax stabilization and to grant Mortgage Recording Tax (MRT) and Sales Tax exemptions. In this capacity, NYCIDA assists industrial, commercial, and not-for-profit organizations in accessing long-term, low-cost financing to acquire or create capital assets, such as purchasing real estate, constructing or renovating facilities, and acquiring new equipment.

NYCIDA facilitates financing through a variety of discretionary bond programs, which include the issuance of triple tax-exempt Industrial Development Bonds; the Exempt Facilities Bond Program, available to companies developing facilities on publicly-owned docks and wharves, or solid waste recycling facilities; and the New York Liberty Bond Program for construction of and major capital improvements for commercial and retail facilities within Lower Manhattan and all New York City. In addition, NYCIDA offers industrial incentive, commercial tax incentive, and financial incentive programs. In general, these programs are designed to provide for economic growth and to induce companies to undertake major capital investments that can result in the creation and retention of significant levels of jobs within New York City.

NYCIDA benefits are discretionary and intended to assist projects that meet New York City goals and would be beneficial to the City. According to NYCIDA's project application process, to be considered for benefits, a company must first make an inducement argument, demonstrating that without the incentives, the project would not occur as proposed. All applicants must also satisfy eligibility requirements and demonstrate a need for assistance. In addition, NYCIDA's governing laws require that companies applying for tax exemption and other City benefits must meet certain economic development criteria, the most important of which is job creation and/or retention in the City. Under other economic criteria, project obligations are intended to help turn around depressed areas, improve quality of life, and increase the tax base.

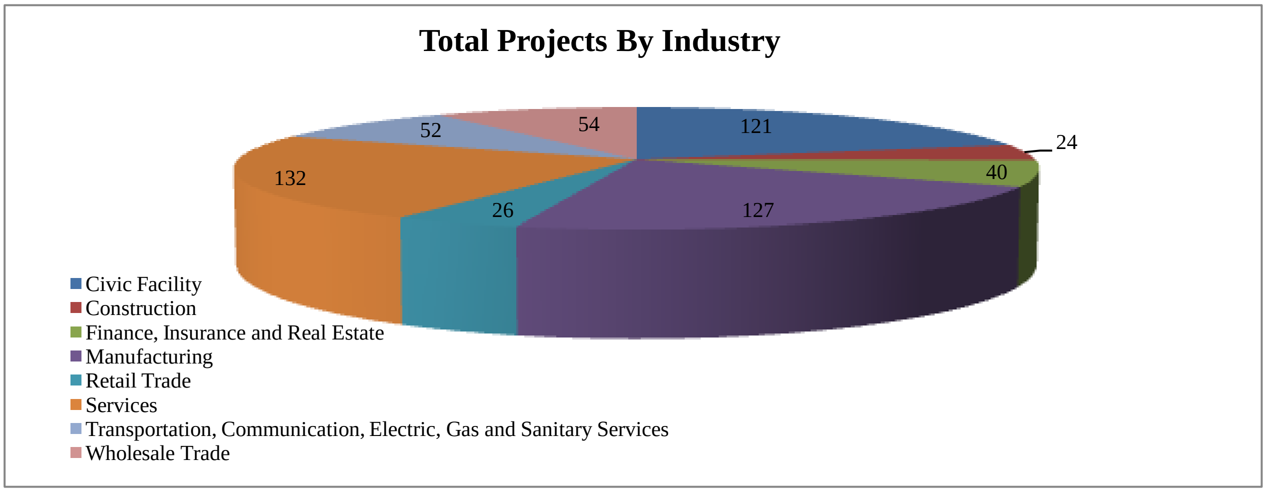
NYCIDA is managed by a Board of Directors (Board[1]). Under the GML, the Board is responsible for establishing its own UTEP criteria for approving or denying all projects. The GML also provides the Board with the authority to recapture economic benefits or impose sanctions or penalties against projects that are not in compliance. Imposition of the recapture policy can require the project owner to return all or part of the value of the tax exemption benefits received. According to NYCIDA's adopted UTEP guidelines, "[u]pon occurrence of a recapture event occurring during a recapture period, there shall occur recapture of Financial Assistance by the Agency. The recapture period shall commence at Closing and shall expire on the tenth anniversary of the Operations Commencement Date" for industrial projects. The guidelines also state that for "Commercial Growth Projects and Governmental Bond Projects, the recapture period shall be determined by the Staff in its sole discretion upon approval by the Board." NYCIDA contracts with the New York City Economic Development Corporation (NYCEDC) for staffing and administrative services.

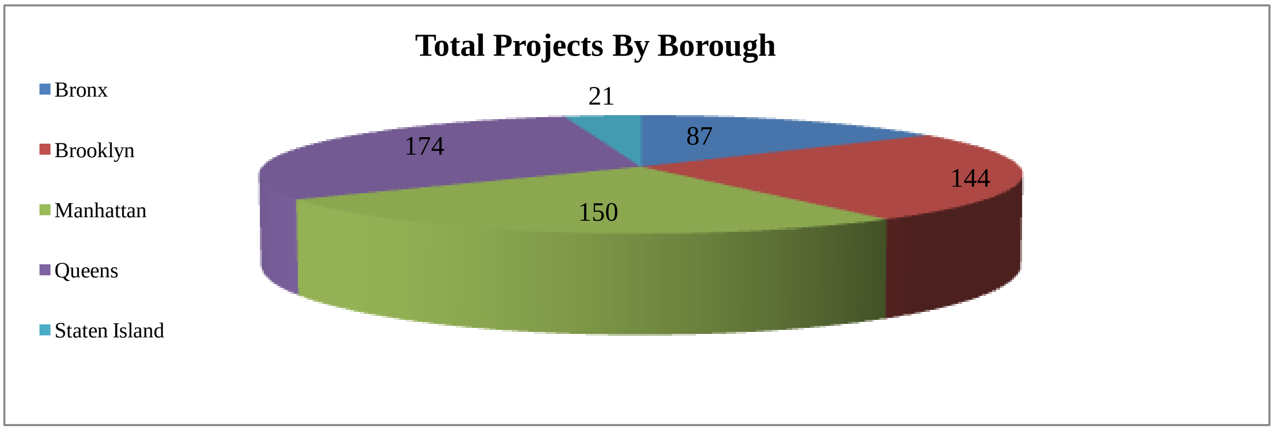
Further, NYCIDA is required to comply with certain reporting requirements, including the annual submission of the Public Authority Reporting Information System (PARIS) report. IDAs are required to file this performance report with the Office of the State Comptroller within 90 days after the close of their Fiscal Year. In its 2009 PARIS report, NYCIDA reported a total of 576 projects with total PILOT payments in the amount of $345.7 million and $497.3 million in tax exemptions[2], including State and City Sales Tax and MRT exemptions.

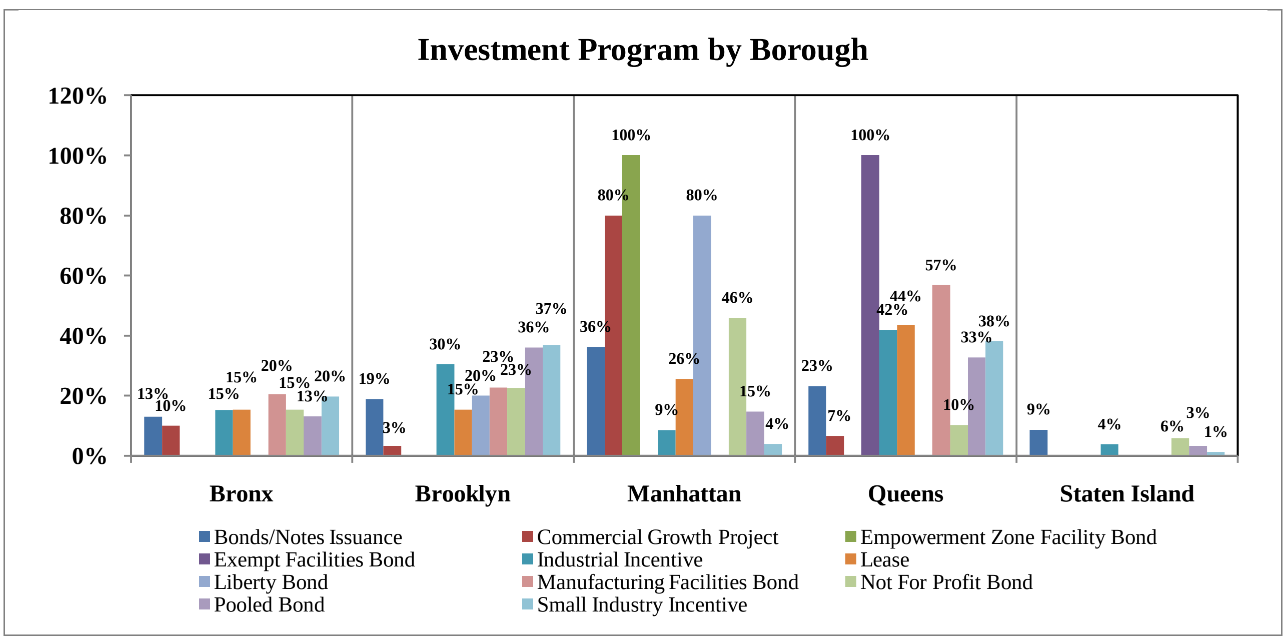
The following charts illustrate project information by depicting total projects by type of industry and borough as well as investment program by borough for Fiscal Year 2009.

[1] The Board consists of 15 members, the majority of whom are appointed by the Mayor. Four of the 15 members are ex officio members. The president of NYCEDC also serves as the chairman of the NYCIDA Board.

[2] This amount included a total of $7.7 million in Sales Tax benefits utilized by Yankee Stadium, LLC, Queens Ballpark Company, LLC, and Bank of America Corporation in Fiscal Year 2009, and was excluded from NYCIDA's re-certified PARIS report covering the same period. The original PARIS report presented a total of $27,088,258 in Sales Tax exemption benefits.


Total Projects By Industry
121
24
40
127
26
132
52
54
Civic Facility
Construction
Finance, Insurance and Real Estate
Manufacturing
Retail Trade
Services
Transportation, Communication, Electric, Gas and Sanitary Services
Wholesale Trade


Total Projects By Borough
Bronx
Brooklyn
Manhattan
Queens
Staten Island
21
87
144
150
174


Investment Program by Borough
120%
100%
80%
60%
40%
20%
0%
Bronx
Brooklyn
Manhattan
Queens
Staten Island
Bonds/Notes Issuance
Commercial Growth Project
Empowerment Zone Facility Bond
Exempt Facilities Bond
Industrial Incentive
Lease
Liberty Bond
Manufacturing Facilities Bond
Not For Profit Bond
Pooled Bond
Small Industry Incentive

Objectives

The objectives of our audit were to determine whether NYCIDA: appropriately evaluated, approved, and monitored project performance; accurately determined and reported the benefit and incentive amounts such as the project employment data and other benefits due to the City; and complied with the provisions of the General Municipal Law and the reporting requirements established under the Public Authority Accountability Act.

Scope and Methodology Statement

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS), except for organizational independence as disclosed in the following paragraph. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

We are issuing this modified GAGAS compliance statement because of the Comptroller's mandated non-audit responsibility regarding NYCIDA. The Comptroller is a member of the Board of Directors of NYCIDA. The Comptroller maintains this position pursuant to New York State General Municipal Law §917-d, which requires that the Comptroller, as the City's chief fiscal officer, be a member of the Board of Directors of NYCIDA. Accordingly, the bylaws of NYCIDA specify that the Comptroller be a member of the Board. The Comptroller participates on the Board of NYCIDA through a designee. The Comptroller's designee was not involved in planning or conducting this audit or in writing or reviewing the audit report.

The scope of this audit was Fiscal Year 2009. Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with NYCIDA officials during and at the conclusion of this audit. A preliminary draft report was sent to NYCIDA officials on November 23, 2011, and was discussed at an exit conference held on December 15, 2011. On January 12, 2012, we submitted a draft report to NYCIDA officials with a request for comments. We received a written response from NYCIDA on January 27, 2012.

In their response, NYCIDA officials disagreed with the report's findings and asserted that:

- "Agency Staff and Outside Experts Conduct Significant Financial and Other Due Diligence Prior To Presenting Any Project to the NYCIDA Board of Directors."
- "The Agency Rigorously Monitors all Existing Projects."

- "The Agency Aggressively Pursues its Legal Remedies When Projects Fail to Meet Their Obligations."

Contrary to these assertions, we found that NYCIDA project files lacked required information and adequate project data, which precluded NYCIDA from conducting meaningful analyses of prospective projects. Furthermore, NYCIDA did not adequately monitor project compliance because it failed to ensure that required employment reports, forms, and certificates were submitted. Moreover, even when documentation was submitted, NYCIDA staff did not visit project locations or undertake due diligence testing to verify the accuracy of reported data. As a result, NYCIDA was unaware that a significant number of projects were not compliant with the terms of their agreements. Finally, NYCIDA failed to seek appropriate remedies when projects were in default or otherwise failed to meet their contract obligations. Most notably, nearly $14.4 million was foregone because NYCIDA did not enforce "recapture and termination" provisions in the case of Bear Stearns, one of the entities that defaulted.

NYCIDA also contended that:

> "In addition to its own due diligence, as a conduit issuer, NYCIDA relies on technical expertise provided by underwriters, placement agents, third-party advisors and bond purchasers. . . . The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

NYCIDA's concern that it may be inappropriate to "usurp" the role of consultants, financial advisors, underwriters, placement agents, and borrowers is misplaced. First of all, entities such as these have a vested interest in obtaining City benefits. Furthermore, NYCIDA's reliance on underwriters, placement agents, third-party advisors, and bond purchasers to perform financial analyses fails to provide adequate assurance to safeguard the City's interests in ascertaining the economic viability of prospective projects. Moreover, our audit found that many project analyses were insufficient, unsubstantiated, or unsound. For example, the Bronx Parking Feasibility Study was flawed because projected revenues were based on questionable occupancy rates and inflated attendance figures and did not account for demand fluctuations that would result from price increases and competition. Accordingly, NYCIDA must conduct independent analyses to ensure that City tax benefits are granted only to those companies that will, in fact, create jobs and comply with their financial obligations.

The full text of the written comments from NYCIDA is included as an addendum to this report.

FINDINGS

NYCIDA generally complied with the Public Authority Accountability Act reporting requirements and filed its PARIS report on time. However, our review found several deficiencies in NYCIDA's review, evaluation, and monitoring of its sponsored projects. Specifically, contrary to NYCIDA's own internal Project Checklist, NYCIDA did not conduct independent analysis of the applicant's ability to meet all equity and debt requirements associated with the projects. In addition, our review found no evidence that NYCIDA verified the accuracy of the data submitted in the project applications. In 36 out of 39 reviewed projects, the information provided was either insufficient or unsupported. As a result, NYCIDA could not be assured that certain proposals were viable and able to achieve the employment goals established in their project applications, which would have a direct impact on the economic development of the area in the City.

We also found that NYCIDA did not follow its own internal procedures to properly monitor project compliance to determine whether companies reported accurate employment data and Sales Tax exemption benefits and whether the projects were operating as intended. As a result, NYCIDA could not be assured that certain significant projects have fulfilled their promises and were entitled to retain their City benefits.

Further, NYCIDA did not initiate the benefits recapture process and ensure that projects were terminated in a timely manner and according to provisions of the project agreements. As a result, the City did not receive the anticipated return on the benefits it invested in the projects and continued to provide benefits to projects in default. Based on our review of NYCIDA's financial records and related project files, we estimate that at least $16,184,760 in unclaimed recapture benefits involving five companies was lost.

These matters are discussed in greater detail in the following sections of this report.

Inadequate Review and Evaluation of Project Information

NYCIDA did not independently evaluate the financial data, purposes, and viability of proposed projects to ensure the projected benefits, in terms of employment goals and tax revenues to the City, could be attainable. Our review of the application files for 39 sampled[3] projects, representing the highest amount of exemptions ($195,962,334) and reporting the lowest employment number (a loss of 3,488), found that for 36 projects the information provided was either insufficient or unsupported. In addition, contrary to NYCIDA's internal Project Checklist, our review did not find evidence of independent data verification or additional analyses performed by NYCIDA to ensure the financial data reported would support future project benefits.

[3] For this test, we judgmentally selected a sample of 42 (16 commercial and 26 non-commercial) projects of the total 576 projects reported in PARIS for Fiscal Year 2009. The 42 sampled projects represent the highest amount of Sales Tax exemptions and the lowest number of employment data reported. Because three of the application files were unavailable, we were only able to review 39 application files.

As noted in our review, NYCIDA uses Regional Input-Output Modeling System (RIMS)[4] to generate a cost-benefit analysis to project the economic impact of projects. However, the components of this analysis are based on projected data. Without a proper process in place to independently review the relevance and adequacy of submitted data upon which the projected data is based, NYCIDA could not properly assess a project's feasibility. Consequently, a NYCIDA recommendation for project approval could result in projects that ultimately fail to carry out the intended purposes, sustain the operations as proposed, or meet the employment expectations to justify all the benefits received. As discussed in the following examples, NYCIDA did not conduct a separate review to authenticate the projected data reported by the project and ensure the financial information submitted would support future project goals.

> ***NYCIDA Response:*** In addressing this finding, NYCIDA stated that "[p]roject managers consistently complete the steps contemplated in this section of the checklist in advance of presenting projects to the NYCIDA's Board of Directors.
>
> "It is worth noting that the Agency collects an extensive list of project and supporting data in order to conduct a cost-benefit analysis and analyze the environmental impacts of a proposed action, in each case, as required by statute. Furthermore, for each project Agency staff conducts additional due diligence, including confirming financing commitments, reviewing the background and experience of the applicant and its principals and assessing the reasonableness of financial projections."
>
> ***Auditor Comment:*** Although NYCIDA properly collected required project data, the information provided was either insufficient or unreliable and was not independently verified by NYCIDA staff. Notwithstanding NYCIDA's contention, project files lacked appropriate evidence to show that NYCIDA staff confirmed financing commitments, reviewed applicant backgrounds and experience, and assessed the reasonableness of financial projections. Accordingly, NYCIDA could not properly assess the viability of prospective projects.

Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc.

Our review found that NYCIDA did not properly evaluate a $19 million project proposal for financing the renovation of a healthcare facility prior to its approval in 2006. The project, Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc. (Wartburg), located in Brooklyn, required NYCIDA's Tax Exempt Bonds to be used as follows: $12 million loans to refinance the facility, $3 million for a new co-generation system, $3 million for the renovation of a new 30-bed Medicaid Assisted Living Facility, and $1 million for closing costs.

NYCIDA was unable to identify certain questionable issues from the project application when it conducted its review of the project. Specifically, NYCIDA did not properly assess the performance of this facility that, according to its own financial records, had been operating at a

[4] Regional Input-Output Modeling System (RIMS) is used by NYCIDA to quantify the economic and fiscal impact of the investment projects.

loss of $1,559,188 in 2004, $740,231 in 2003, and $2,086,202 in 2002. According to NYCIDA's internal Project Checklist, a significant requirement for a certain project's eligibility is that the project can demonstrate the ability to generate a positive cash flow. However, NYCIDA did not follow its own Checklist in ensuring that this company was not facing cash flow issues that would hinder its ability to service the proposed debt. Instead, NYCIDA justified its decision to approve this project by noting that the negative free cash flow was due to major capital renovation costs on the healthcare organization's existing facility. Based on the project's financial statements information, there was no corresponding increase in fixed assets related to any such capital expenditure amount reported. In addition, as the records disclosed, the reason for the deficits was mostly due to the changes in the healthcare industry as a whole and the company's inability to obtain reimbursement funds from Medicare and Medicaid patients as a result of not meeting the occupancy threshold required by the State. Without taking all these key factors into consideration, NYCIDA could not have properly assessed this company's ability to meet its cash flow requirements going forward. Consequently, the City lost the value of the tax benefits granted.

Our review of the project documents also found that, although the project obtained NYCIDA's financial tax incentives, it failed to deliver the expected benefits. As project documents revealed, as soon as the installations of the new co-generation system, boilers, and generators were completed and the $3 million in installation costs were paid in February 2008, the facility holder notified NYCIDA of its decision to sell the facility. The agreement was terminated and the bonds ($18.6 million) were paid in full by Wartburg as of September 9, 2008. Nevertheless, the facility never had the renovation work done for the new 30-bed Medicaid Assisted Living Facility as promised in the project application. With the low interest rates and tax exemptions granted by NYCIDA's project financing program, the facility benefited from at least $2,669,749 in interest and tax savings for approximately $2 million in net cost savings and benefits as shown in Table I.

Table I
Estimated Interest and Tax Savings Benefited by
Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc.
from NYCIDA's Financing Program

	Interest Rates p.a. (%)					
Period	Bonds (I)	Mortgage (II)	Loan (III)	Bond Principal (IV)	Interest Rate Differential (%) V=(II or III – I)	Interest Differential (IV*V*27mths)
6/2006-9/2008	2.92	6.61		$ 10,393,485	3.69	$ 862,919
6/2006-9/2008	2.92		8.02	$ 6,771,515	5.10	$ 777,031
Subtotal				**$ 17,165,000**		**$ 1,639,950**
6/2006-9/2008	4.13		8.02	$ 1,435,000	3.89	$ 125,598
Total				**$ 18,600,000**		**$ 1,765,548**
Add: Income Received from the Trust Account						$ 345,278
Add: City and State Benefits						$ 558,923
Total Interest and Tax Savings						**$ 2,669,749**
Less: Closing Fees						$ 737,277
Net Cost Savings and Benefits Gained by the Project						**$ 1,932,472**

(I) Average of the Variable Rates - Maximum and Minimum for FY 2008 - for NYCIDA Bonds issued for the facility.
(II) Monthly average for June 2006, provided by the HSH Associates, the nation's largest publisher of mortgage information.
(III) Business loans interest rate for June 2006 provided by the Board of Governors of the Federal Reserve System.

NYCIDA Response: "These findings are factually incorrect. First, in accordance with the Agency's UTEP, the Agency collected all relevant financial and other supporting data to conduct the reviews described in the prior response. In addition, in reviewing the project, the Agency considered the financial strength of both Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc. (an affiliate of the borrowing company). Second, negative cash flows were analyzed by NYCIDA staff but were, in part, explained by a large and non-recurring renovation to their facility. The Audit Report's statement that no evidence existed in Wartburg's audited financials as to this investment is incorrect as Wartburg's financial statements indicated that the organization's fixed assets increased by over $1mm during the period between 2003 and 2004 due to the renovations/ improvements. Additional increases in net assets would have appeared on the statements but were offset by depreciation during the same period. Third, the Agency did not ignore changes to Medicare and Medicaid reimbursements and disclosed such changes in the materials provided to the Board of Directors.

". . . the Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

Auditor Comment: As stated in the audit, project financial statements did not indicate a corresponding increase in fixed assets that could possibly account for negative cash flows between Fiscal Years 2003 and 2004. In any case, project records showed that the deficits were largely attributable to changes in the healthcare industry and the company's inability to obtain reimbursement funds from Medicare and Medicaid patients. Moreover, the reimbursement figures provided to the NYCIDA Board of Directors were not properly analyzed and considered in evaluating the project's financial feasibility.

NYCIDA again points out that it relies on other parties to ascertain the financial viability of projects. However, as stated previously, reliance on entities that have a vested interest in obtaining City benefits (e.g., underwriters, placement agents, third-party advisors, and bond purchasers) to perform financial analyses fails to provide adequate assurance to safeguard the City's interests in ascertaining the economic viability of prospective projects.

Bronx Parking Development Company, LLC

Our review of the Bronx Parking Development Company, LLC (Bronx Parking) project application records found that NYCIDA did not ensure that its staff gathered sufficient information that would allow it to make a well-informed recommendation to the Board for the approval of this project on October 9, 2007. A key provision of NYCIDA's internal Project Checklist requires that NYCIDA conduct an "[i]ndependent analysis of the applicant's ability to meet all equity and debt requirements associated with the project." However, NYCIDA did not independently analyze the financial position and cash flow of the proposed parking operation or the parking needs of the community to determine if there would be a demand for increased parking, at higher prices, in the Yankee Stadium vicinity. As reported, the original parking facility had a capacity of 7,425 parking spaces, and Bronx Parking was requesting benefits consisting of $225 million in bond financing and $70 million and $39 million from State and City investments, respectively, to create an additional 2,184 parking spaces for a total of 9,609 parking spaces.

Further, as we noted in our review of the 2006 Final Environmental Impact Statement (FEIS) prepared in connection with the construction of the adjacent Yankee Stadium, there were 7,425 available current parking spaces and only 7,276.5 (98 percent) occupied for a weekend game, and 7,128 (96 percent) for a weeknight game. This occupancy was based on a 54,000 attendance sellout game at the old Yankee Stadium with its 57,000 attendance capacity. However, as reported at the time, the new Yankee Stadium, which opened in April 2009, would have a reduced capacity of 50,000, which would correspondingly reduce demand for parking.

In addition, the August 2007 modification to the FEIS reflected a reduction in the original parking space usage based on possible changes in customer demand in the long run due to the increased competition. However, despite the reduction in the new Stadium capacity and the anticipated decrease in customer demand due to the simultaneous potential developments of other parking facilities in the proximity of the new shopping center and the proposed Metro North station in the area, Bronx Parking still proposed in its December 2007 Feasibility Study its projected rates based on 8,527 parking occupancy as summarized in Table II:

Table II
Summary of the Parking Rates Projected for 2009 and 2011 by the Bronx Parking Development Company, LLC

Users	Projected 2009 Rate	Projected 2011 Rate	Percentage of Increase
Season Passholders	$ 17.10	$ 27.00	57.89%
Non-Season Passholders	$ 19.00	$ 30.00	57.89%
Valet	$ 32.00	$ 42.00	31.25%

Note: The actual rates for 2011 were $35 for Non-Season Passholders and $48 for Valet Parking

As the project data illustrates, with the projected increase in rates for self-parking over 57 percent in two years (2009-2011), Bronx Parking was at risk of losing its competitiveness, both to other surrounding parking facilities, which charged only $23 for 2011, and to the free on-street parking in the community, the congestion of which the new proposed parking was meant to alleviate. In light of the publicly available information, NYCIDA should have independently assessed whether Bronx Parking's estimates of expected parking revenues were realistic, taking into account the rather optimistic estimates of parking needs and the sharply increased parking fees that would need to be charged.

NYCIDA determined the viability of the project based on a narrowly scoped RIMS analysis of the costs and benefits to the City and the State, assuming that the parking operation would be able to sustain itself and meet the anticipated project goals and provide related benefits.

While a Feasibility Study prepared by a Bronx Parking consultant in connection with the project financing was available, its analysis of the future parking demands focused mainly on the existing Yankee Stadium attendance records and the current parking capacity and rates. Also, as the Feasibility Study revealed, neither the number of valet spaces nor the average number of valet and non-valet transactions recorded in 2006 was documented or available.

Further, NYCIDA did not ensure that the most cost-effective plan for the proposed parking spaces as cited in the 2006 FEIS was selected. In particular, although the FEIS discussed a low maintenance plan that would combine the existing parking spaces with the 1,200 parking spaces made available through the expected new shopping center, for a total of 7,859 parking spaces, this option was never considered.

As a result, the assessment of this project was not sufficiently detailed and inclusive to determine if there was a reasonable expectation that the $334 million project investment would: retain the demand as forecasted and generate enough revenue to pay off its debt service; remit the anticipated rent and PILOT revenue to the City; create and retain the number of full-time and part-time jobs promised; and, most significantly, deliver the economic growth to the Bronx community as part of the overall project objectives stated in the inducement argument it presented in the application. Further, NYCIDA did not look for alternatives that would safeguard the sustainability of the project by either dividing the project into phases or selecting designs that would allow future usage or redevelopment alternatives if the parking garage's full capacity was not reached.

As of December 31, 2010, the Bronx Parking project still owed the City $17,775,808 in outstanding principal and interest on rent and PILOT payments. In addition, we were not able to determine, based on agency documentation, whether the project has generated the 20 full-time and 70 part-time anticipated employment benefits in the area. The project also has outstanding bonds payable in the amount of $237,635,000 and $3,448,689 in related bond interest. Further, from Fiscal Years 2008 through 2010, the project received total public funding of $70,000,000 from the Empire State Development Corporation and $39,162,852 from NYCEDC. Therefore, in its capacity to recommend to the NYCIDA Board that NYCIDA assist worthwhile projects, NYCIDA staff was not diligent in ensuring the information submitted could sustain the purposes intended and ultimately return the intended benefits.

> ***NYCIDA Response:*** "The Agency disagrees with the finding that NYCIDA did not ensure that its staff gathered sufficient information to allow it to make a well-informed recommendation. The Bronx Parking Development Company project was financed following the completion of an extensive independent third-party parking system feasibility analysis, conducted by Desman Associates, a nationally recognized expert in that field. The study included a 'review and analysis of the current and projected demand for parking in the vicinity of the Yankee Stadium, the multi-year parking revenue projections, the operation/maintenance budget and the long-term capital repair and replacement expense budget' (Desman Report, Page 1) for the project. This study was included, with the consent of Desman, in the Official Statement presented to prospective bond purchasers. In addition, contrary to findings in the Audit, the Agency did analyze and adopt findings under the State Environmental Quality Review Act which specifically

addressed the issue of a reduction in required parking spaces needed for the project as the result of the construction of a new MetroNorth commuter rail station adjacent to the new Yankee Stadium. This reduction in parking spaces was also reflected in the independent feasibility analysis completed by Desman. Again, the Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

Auditor Comment: The Bronx Parking Feasibility Study was flawed because projected revenues were based on questionable occupancy rates and inflated attendance figures and did not account for demand fluctuations that would result from price increases and competition. Moreover, according to the study's disclosures, "Neither the number of valet spaces nor an average number of valet and non-valet transactions recorded in 2006 were documented or available." Furthermore, the study did not indicate how the parking operations would create and sustain 20 full-time and 70 part-time jobs. We again emphasize that it is imprudent and inappropriate for NYCIDA officials to rely mainly on applicant and investor supplied analyses that significantly impact the City's economic development, as these parties have a vested interest in securing City benefits.

Hollow Metal Factory Outlet Corp.

In another instance, our review of the project file of a newly created distributor of metal doors located in Brooklyn found that the project, Hollow Metal Factory Outlet Corp., was approved in 2000 for a financial initiative that offered total net present value of $462,575 in various City tax exemptions related to its new facility. According to the final records submitted with the project application, the project reported projected income statements for the first two years including $24,793 and $170,870 in net income, and $2,407 and $16,590 in provision of corporate taxes, respectively. The application also anticipated creating 10 jobs within three years of the closing date. However, based on the above data that we reviewed, the projected profits and resulting corporate taxes were too minimal to justify NYCIDA's decision to grant the aforesaid tax benefits. Furthermore, the project never attained the anticipated employment growth or even hired more than two employees. As of February 16, 2009, shortly before the voluntary project termination, the project received total tax benefits of $295,819 with an average City cost of $147,910 per job created or three times the $46,258 per job as estimated upon project approval. NYCIDA's inability to address the anticipated employment level cited in the application and the consequential recourse available in its lease agreement obviously derails the City's goal to enhance employment in exchange for all forgone City benefits.

NYCIDA Response: "The Agency disagrees with the assertion that the projected profits and resulting corporate taxes were too minimal to justify NYCIDA's decision to grant tax benefits. The company's projected tax liabilities such as corporate and payroll taxes are not the only factor used to determine a project's validity. The standard cost-benefit analysis, which is one component of the analysis performed as part of all project reviews, takes into account a wide range of fiscal impacts to determine if tax incentives should be provided. A full cost benefit analysis was performed, using the industry standard model, and showed a positive return to the City from the proposed project."

Auditor Comment: Project files lacked documentation to substantiate NYCIDA's contention that factors other than the company's projected tax liabilities were used to determine the project's viability. There was no evidence that NYCIDA conducted a cost-benefit analysis.

Inadequate Project Monitoring

Employment Levels Not Achieved

Our review of NYCIDA's compliance submissions for 16 sampled major commercial projects found that seven (44 percent) of the projects reviewed fell below the base employment number stipulated in their project agreements as summarized in Table III. Under the terms of the project agreements administered by NYCIDA, companies can lose future benefits if their employment number falls below certain pre-established levels. Because other economic factors may trigger a company's employment number to be below the required amount and because job creation is a significant requirement for the approval of certain projects, NYCIDA should review the threshold percentage allowed to each commercial project to encourage companies to maintain a more desirable employment level.

Table III
Summary of Sampled NYCIDA Projects Below Base Employment Requirement
Fiscal Year 2009

Project Name	Base Employment Requirement	Eligible Employees for FY 2009	Variance	Percentage Below
The Bear Stearns Companies, Inc. (JP Morgan Chase & Co.)	5,700	3,649	(2,051)	(36%)
The Depository Trust Company	2,799	2,235	(564)	(20%)
Information Builders, Inc.	818	667	(151)	(18%)
Merrill Lynch & Co., Inc.	9,000	8,584	(416)	(5%)
Time, Inc.	4,350	2,879	(1,471)	(34%)
Viacom, Inc. (CBS Corporation)	4,808	1,521	(3,287)	(68%)
VNU USA, Inc. (TNC (US) Holdings, Inc.)	1,157	977	(180)	(16%)

NYCIDA Response: "The Agency disagrees with the assertion that NYCIDA should review the threshold percentage allowed to each commercial project in order to encourage companies to maintain a more desirable employment level. The employment threshold percentages are established in Project Agreements to account for general fluctuations in employment levels that are part of a company's usual course of business. As documented in the Project Agreements, significant employment declines may be cause for termination or recapture. However, more minor and/or cyclical fluctuations do not necessarily trigger such penalties. As became evident in 2008, employment declines for many companies were an unavoidable result of a global economic recession. We believe the thresholds established in the Project Agreements strike a fair balance between ensuring the City realizes the employment benefits it anticipates while not penalizing companies for employment changes that are a normal part of running a business. Where applicable, the NYCIDA Compliance Department ('Compliance') enforced available remedies . . ."

Auditor Comment: Our concern was that for seven of the 16 sampled major projects, employment levels were significantly lower than those established in the project agreements. NYCIDA did not monitor fundamental project compliance because it did not ensure that employment reports, forms, and certificates were submitted. As a result, a significant number of major projects were not compliant with their agreements. As noted, our review found that required employment forms were not submitted for more than 57 percent of sampled projects. In addition, NYCIDA did not ensure that Bear Stearns created and sustained the remaining 3,474.5 of 5,700 jobs (61 percent) required by its project agreement.

Did Not Adequately Monitor to Ensure Job Retention Requirements Were Met

NYCIDA did not adequately monitor project compliance with the job requirements. Our review of 42 project compliance files noted that although NYCIDA requires projects to submit an Employment and Benefits Report (EBR) quarterly NYS-45 Form and annual employment certificate, it did not verify whether the reported employment data was accurate and in compliance with the project agreements. Further, NYCIDA did not ensure that all required employment reports were submitted. Specifically, our review of NYCIDA's compliance records found that of the 42 project files reviewed, the required NYS-45 Forms were missing in 24 (57.1 percent) projects, which included six of the seven projects noted above. In addition, we found that EBRs were not submitted in six (14.3 percent) of the total compliance files reviewed, which included one of the seven projects noted above. Of the six projects that did not have the EBRs, only one project received a Notice of Non-Compliance. Without verifying the data in the available employment reports and obtaining all required reports, NYCIDA could not be assured that the companies are in compliance with their project agreements.

NYCIDA Response: "The Agency disagrees with the finding that the NYCIDA did not adequately monitor project compliance with job requirements. The audit states that of the 42 projects sampled, six (or 14.3%) did not submit an Employment and Benefit Report (EBR). However, five of those six projects were terminated during FY2009. Companies are not required to submit their annual EBR if they no longer have an active agreement with NYCIDA at the end of the fiscal year . . ."

Auditor Comment: Contrary to NYCIDA's assertion, terminated projects are still required to submit their EBR as of the project termination date. Of the five terminated projects listed in NYCIDA's response, Hollow Metal submitted its EBR as of the project termination date, but the other four projects did not. Therefore, it is important that

NYCIDA ensures that all employment data is currently reported when a project is fully terminated. Based on our review, NYCIDA did not do so.

NYCIDA Lacks Controls over the Use of Sales Tax Letters

Our review of the Sales Tax Letters noted that NYCIDA allowed both the originals and copies of a Sales Tax Letter to be acceptable for claiming Sales Tax exemption from vendors, which, in turn, may allow the Sales Tax benefits to be continuously obtained even when the original letter has been recalled for suspension or cancellation. In view of the over $27 million in total Sales Tax exemptions NYCIDA granted in Fiscal Year 2009, NYCIDA needs to develop better control procedures to safeguard the Sales Tax Letters from being misused by ineligible users. NYCIDA should also verify that the amounts reported are accurately and completely reflected in the project records to ensure the proper recapture calculations when a project is in default.

NYCIDA Response: "The Agency disagrees with the finding that NYCIDA lacks controls over the use of sales tax letters. NYCIDA works in close collaboration with New York State Department of Taxation and Finance ('NYSDOTF') to administer sales tax letters in accordance with general practice and sales tax exemption procedures. All NYCIDA sales tax letters are reviewed and renewed annually and have a clear expiration date. Each letter also provides details of eligible purchases and locations. When the letter expires, is cancelled due to non-compliance, or if benefits are terminated before the letter's expiration date, Compliance requests that the original letter be returned.

"In the event of unauthorized use by a project company, NYCIDA, in conjunction with the NYSDOTF, pursues corrective action, which typically results in repayment of benefits and/or interest and penalty, if applicable. Furthermore, project companies, their contractors and their vendors are subject to audit by NYSDOTF.

"In addition to the above controls for use of sales tax letters, all projects with an active sales tax letter are required to file an ST-340 form with NYSDOTF (with a copy to NYCIDA) detailing the exemptions claimed in a given calendar year. These are aggressively collected and monitored by Compliance in addition to NYSDOTF. For calendar year 2010, the most recent date the form was due to the State, 96% of all projects sent copies to the Agency.

"Finally, the Agency's Commercial Growth projects are required to submit a detailed registry for all purchases made utilizing the sales tax letter. These are carefully reviewed by Compliance to verify project purchase eligibility and benefit usage. In addition, most commercial growth projects are required to submit tri-annual reviews of their purchases performed by certified public accountants and are always subject to audit by NYSDOTF should one be requested."

Auditor Comment: If NYCIDA is confident that it has sufficient procedures to preclude the unauthorized use of sales tax letters, it should ensure that these procedures are fully implemented. However, as discussed in the audit, NYCIDA could not track the use of unauthorized sales tax letters and permitted their use even after projects had been terminated.

Did Not Conduct Periodic Site Visits

Our review of all 42 sampled project files found that NYCIDA did not conduct periodic site visits to authenticate the reported employment and the capital investments related to the Sales Tax benefits obtained and to determine whether the premises are in operation as intended. As a result, NYCIDA could not identify defaulting projects and discontinue their benefits in a timely manner.

NYCIDA Response: "The Agency disagrees with the finding that periodic site visits are not performed to NYCIDA project locations to authenticate employment and capital investments. It is true that of the 42 projects the Comptroller's Office sampled, a very small number received site visits in FY 2009. However, the selected sample simply is not representative of the Agency's oversight of its entire portfolio of projects, either in FY2009 or in subsequent years. Compliance conducted 44 site visits in FY2009, 75 in FY2010, and 119 in FY2011.

"Starting in FY2012, Compliance commenced a five-year self-audit plan in which 20% of the portfolio (about 105 projects as of FY2012) will be thoroughly reviewed each year, including, but not limited to, an on-site field visit inspection. In combination with our pre-existing site visit policies the Agency expects to, and are indeed on pace to, perform significantly more site visits than the 120 performed last year."

Auditor Comment: Although we cannot attest to the efficacy of NYCIDA's prospective program to annually audit and inspect 20 percent of projects, it could be an important step in remedying the deficient number of site visits that NYCIDA did not conduct for the sampled projects.

NYCIDA Did Not Initiate the Benefits Recapture Process and Ensure that Projects Were Terminated in a Timely Manner, Resulting in at Least a $16,184,760 Loss in City and Other Benefits

NYCIDA failed to enforce the benefits recapture and termination provisions stipulated in the project agreements that resulted in a loss of at least $16,184,760 in tax and other benefits from five defaulted projects. Specifically, based on our review of the project records, NYCIDA did not document its decision or outline criteria to justify why certain projects would not be subject to the recapturing provisions. According to NYCIDA's UTEP guidelines, "[u]pon the occurrence of a recapture event in respect of a Commercial Growth Project or Governmental Bond Project, the Agency shall recapture such Financial Assistance, together with such interest, as Staff determines in its sole discretion upon approval by the Board." Our review of 42 sampled projects found that NYCIDA did not recapture benefits from five projects that it should have as follows:

$14,374,960 in Forgone Benefits Recapture Due to Project Non-Compliance

Our review of the project termination documents involving The Bear Stearns Companies, Inc., located in Manhattan, found that NYCIDA made a decision not to enforce the provisions of the agreement to terminate the project and recapture the benefits. Specifically, NYCIDA improperly allowed $6,165,291 in tax and energy benefits for Fiscal Year 2009, did not collect benefits totaling $7,297,768 for Fiscal Year 2010, and failed to timely terminate the energy benefits until October 28, 2010. Our review of the project records found that NYCIDA did not document its decision or outline criteria to justify why this project would not be subject to the recapturing provisions.

As project records revealed, on May 30, 2008, company officials voluntarily requested NYCIDA to discontinue the project's Sales Tax Letters as a result of the project being involved in a merger-acquisition transaction. Although the company did not continue to use the Sales Tax Letters, it still continued the use of the energy benefits granted by NYCIDA. In 2009, NYCIDA accepted a request from JP Morgan Chase & Co. (JPMC), the successor company, to reinstate the Sales Tax Letters for transactions retroactive to May 30, 2008. According to the employment data provided by JPMC, the project was still in compliance under the terms of the agreement. Based on this information, NYCIDA reinstated the Sales Tax Letters. However, when the Annual Certificate for Fiscal Year 2009 was finally submitted in August 2010, it reflected that the total number of eligible employees dropped from 6,591.5 in July 2008 to 2,225.5 (39 percent of 5,700 required in the project agreement) in June 2009. Although NYCIDA immediately terminated the benefits, it made a decision that there would be no recapture of any benefits provided for the period July 1, 2008, through June 30, 2009. Our further review of the benefits termination documents revealed not only that NYCIDA allowed JPMC to keep $6,165,291 in total benefits granted in Fiscal Year 2009, but also that NYCIDA relinquished its right to collect total benefits of $7,297,768 for Fiscal Year 2010 and allowed the company to continue to receive the energy benefits until October 28, 2010. The losses in City and energy benefits are summarized in Table IV.

Table IV
City and Other Benefits Forgone for The Bear Stearns Companies, Inc. Due to NYCIDA's Inability to Timely Initiate Benefits Termination

Period	Sales Tax Benefits	Energy Benefits	Property Tax Savings	Total
FY 2009	$ 1,584,777	$ 2,370,514	$ 2,210,000	$ 6,165,291
FY 2010	$ 1,789,445	$ 2,773,700	$ 2,734,623	$ 7,297,768
FY 2011*		$ 911,901		$ 911,901
Total	**$ 3,374,222**	**$ 6,056,115**	**$ 4,944,623**	**$ 14,374,960**

*Our estimation is based on the energy benefits received in FY 2010 pro-rated for the period July 1, 2010, through October 28, 2010.

NYCIDA Response: "The Agency disagrees with the assertion that NYCIDA improperly allowed tax and energy benefits for Fiscal Year 2009. On November 1, 1989, Chase Manhattan Bank (successor in interest to JPMorgan Chase & Co.) entered into a commercial incentive bond transaction with NYCIDA to acquire and maintain designated facilities in what is now known as Brooklyn's MetroTech Center. On September 1, 1999, The Bear Stearns Companies Inc. entered into a commercial incentive straight-lease transaction with NYCIDA to maintain at least 5,700 employees in New York City through 2049 in return for energy benefits, real property tax benefits and sales tax benefits.

"In 2008, in response to an economic downturn, Bear Stearns signed a merger agreement with JP Morgan Chase ('JPMC'). Thereafter, NYCIDA Compliance sent a letter to JPMC asking that they report the details of the merger to the Agency, in accordance with the Project Agreement. Negotiations with JPMC occurred between August 2008 and January 2009 about potential restructuring options for the transaction.

"Under both the IDA Project Agreement and the NYCPUS Power Service Agreement, JPMC, as the successor to Bear Stearns, was entitled to continue to receive energy benefits, real property tax benefits and sales tax benefits. After negotiations with NYCIDA, in August 2010, JP Morgan Chase agreed to terminate NYCIDA Project documents, notwithstanding that a substantial amount in unused sales tax benefits remained available to JPMC under the agreement. In addition, although termination documents were not executed until 2011, JPMC agreed that NYCPUS energy benefits would cease on October 28, 2010. Under the Project Documents, the Agency was not entitled to demand a recapture of benefits based on the reduction in the number of Bear Stearns employees following the Chase's acquisition of Bear Stearns.

"It is also important to note that JPMC's obligations (i) to continue reporting the number of Bear Stearns employees employed by it and (ii) to maintain the headquarters of Bear Stearns Companies LLC, a subsidiary of JP Morgan Chase, in New York City, survived the termination of the Project Agreements and remain in effect. NYCIDA also continues to have benefits recapture rights that may be exercised if JPMorgan Chase relocates Bear Stearns employees or the Bear Stearns headquarters outside of New York City."

Auditor Comment: Contrary to NYCIDA's claim, JPMC was not entitled to receive energy and tax benefits if its employment level fell below 4,275 (75 percent of the threshold of 5,700), as stated in Section 9.3(b) of the NYCPUS Power Service Agreement and Sections 5.5(c) and 5.7(b)(ii)(C) of the Project Agreement.

In addition, project documentation showed that the Bear Stearns project was already in default when its employment level dropped to 2,225.5 in June 2009. Therefore, any benefits granted from Fiscal Year 2009 onwards should have been recaptured. In this case, it was inappropriate for NYCIDA to determine that the eligibility status of Bear Stearns entitled it to obtain public benefits totaling more than $14 million.

Did Not Recapture $520,800 Due to Early Termination

In addition to not properly evaluating the Wartburg healthcare facility (as previously reported), NYCIDA failed to recapture the benefits it granted to Wartburg after the facility was sold. According to §8.5 of the project's Installment Sale Agreement and Assignment of Lease, "[i]n the event the Institution exercises its options to pay in advance all installment purchase payments becoming due . . . and shall thereafter sell all or substantially all of the Facility, or cause all or substantially all of the Facility to be sold within ten (10) years from the date of issuance of the Bonds . . . the Institution shall pay to the Agency as a return of public benefits conferred by the Agency . . . one hundred percent (100%) of the Benefits if the Facility is sold within the first six (6) years after the issuance of the Bonds." Our review found that, although Wartburg paid its outstanding Bond obligations and sold the Facility in May 2010, NYCIDA did not initiate the required benefit recapture action. As a result, it did not recover a total of $520,800 in Mortgage Recording Tax benefits from Wartburg. NYCIDA's records did not document the basis for its decision or criteria used in deciding not to initiate a benefit recapture action.

NYCIDA Response: "The Agency disagrees with the finding that the Agency was required to initiate a benefit recapture action. The Agency did not make a recapture claim against Wartburg Lutheran Home for the Aging and Wartburg Nursing Home, Inc. (the 'Borrower') as the Borrower entered into a Voluntary Receivership Agreement pursuant to Section 2810 of the Public Health Law with the Department of Health. The purpose of Section 2810 is to provide a bankruptcy-type procedure for facilities like the Borrower's not-for-profit nursing home; and the purpose of the procedure is to insure the safety and continued servicing of a needy population.

"In connection with that agreement, the Borrower was under contract to sell its realty and its assets to, respectively, Wartburg Realty LLC and Wartburg Receiver LLC. While the Agency's recapture provisions in the Borrower's agreements with the Agency literally apply to a 'sale' of the project facility, the sale that in fact occurred arose out of distressed circumstances pursuant to a statutory procedure designed to protect a vulnerable population, service continued to be provided to this population and the jobs that the Agency's assistance sought to create continued. It was the Agency's determination that pursuing recapture in such a circumstance did not further the policy objective underlying the original transaction.

"Furthermore, the Wartburg Nursing Home has continued to operate as a full service nursing home at the project location."

Auditor Comment: NYCIDA's confusion about its own interpretation of the issues is an additional indication of its lack of knowledge regarding its role as an oversight agency of the City. Contrary to NYCIDA's assertion, the facility was not "literally" but indeed sold to Wartburg Realty LLC, an independent for-profit entity, in May 2010 and is currently operating as Bushwick Center for Rehabilitation and Health Care. Therefore, NYCIDA's argument is baseless. Whether the sale was prompted by "distressed circumstances" and that "[i]t was the Agency's determination that pursuing recapture in such a circumstance did not further the policy objective underlying the original transaction" was irrelevant insofar as the terms of the lease agreement was concerned. (We also note that at the exit conference, NYCIDA asserted it did not enforce the recapture provisions of the lease agreement for a different reason—that benefit recapture was not feasible because Wartburg was under receivership.)

Improperly Allowed $79,000 in City PILOT Benefits Due to Delay in Termination

Our review of Paradise Products Corp., a food manufacturing company located in the Bronx, noted that NYCIDA confirmed by a site visit[5] on December 13, 2007, that the facility was vacated for resale and no longer in operation. However, NYCIDA did not issue a Notice of Default until January 30, 2009. Although NYCIDA was able to recapture most of the benefits retroactive to December 13, 2007, the delay in the termination process benefited the defaulted company by at least $79,000 in City PILOT benefits until the project was finally terminated on May 7, 2009.

Improperly Allowed $50,000 in City PILOT to a Defaulted Project

Our review of Austin Automotive Warehouse Corp., an automotive company located in Queens, found that the company violated the lease agreement by subleasing the property without prior approval from NYCIDA. A Notice of Default and Recapture Event was first served on January 3, 2008. However, NYCIDA did not terminate the project immediately in accordance with the lease agreement. Instead, NYCIDA negotiated continuously without prospective results and delayed the termination for over two years until April 26, 2010. Although NYCIDA recaptured most of the benefits retroactively back to the date of default, it continued to provide City PILOT benefits of at least $50,000 to the company during the extensive period of negotiation.

NYCIDA Response: "The Agency disagrees with the finding that NYCIDA improperly continued City PILOT benefits to Paradise Products Corp. and Austin Automotive Warehouse Corp. In general NYCIDA strives to expedite benefit suspension and/or terminations to ensure projects are placed back on City tax rolls and incentives cease to accumulate. NYCIDA expeditiously pursues recapture as applicable and appropriate under the Project Documents.

"The Agency also takes the task of supporting businesses and maintaining employment in the City very seriously, and as a result, pursues not only the penalties available under the Project Documents, but also seeks to negotiate with companies in an attempt to preserve jobs and best serve the City as whole. In the aforementioned examples, the Agency ultimately terminated project documents but only after all available options were exhausted for the projects to maintain operations and provide the greatest benefit to the City."

Auditor Comment: Regardless of how long it takes NYCIDA to terminate a project, it should ensure that all benefits, including PILOTs, are recaptured from the time that a project is declared to be in default.

[5] This site visit was not initiated by NYCIDA, but reacted upon a notification of possible sale of the project site.

Improperly Waived $1.16 Million in City Tax and Other Benefits Recapture

Our review of Baldor Specialty Foods, Inc., a food services company located in the Bronx, noted that the project defaulted by moving substantially all of its operations in May 2008 to another facility that was under a separate lease agreement with NYCEDC. Based on a NYCIDA memorandum dated as of March 3, 2009, the company was subject to a recapture of $568,992. However, NYCIDA continued to encourage the company to explore a continuation plan or tenancy plan of the vacant project site. Without any viable plans submitted, NYCIDA finally issued a Notice of Event of Default and Lease Termination on January 22, 2010, and unilaterally terminated the project on October 6, 2010. Not only did NYCIDA delay the termination process for over two years, but it also continued to offer the defaulted entity at least $558,181 in PILOT benefits and ultimately waived approximately $1.16 million in benefits recapture upon project termination. Obviously, NYCIDA did not exercise proper due diligence to ensure that the company develop a continuation plan or tenancy plan prior to the finalization or even the negotiation of the lease agreement with NYCEDC. The inability of the project to comply with and of NYCIDA to enforce the terms of the lease agreement should not be the basis for the City to continue giving away benefits in an Event of Default or for NYCIDA to righteously waive approximately $1.16 million in benefits that should have been recaptured. Therefore, we conclude that, although documented, NYCIDA's basis for waiving the recapture of benefits was unreasonable.

NYCIDA Response: "The Agency disagrees with the finding that NYCIDA improperly waived a recapture of benefits from Baldor Specialty Foods Inc. Baldor outgrew the project facility and was seeking a new location in order to expand its operations and employment. The Company evaluated its options for relocation and concluded that another facility in the Bronx would best serve their needs during expansion. The Company's relocation from its designated project location did technically constitute a recapture event under their Project Agreements. However, given that they were relocating and indeed expanding within the City, it did not serve NYCIDA's policy objective to terminate and recapture benefits of a company that was increasing its commitment to the City. Additionally, under current NYCIDA Board-approved UTEP guidelines this would no longer be a recapture event under the documents (provided they maintain similar employment at the new location).

"The Company has since made significant investments in the new facility while growing its employment from 517 employees in 2007 (original location) to 556 employees in 2009 (new facility), an increase of seven percent."

Auditor Comment: We continue to disagree. The selection of potential tenants to occupy the Hunts Point City-owned property was approved by the Mayor's office in December 2005. After such approval, Baldor signed a 20-year ground lease with NYCEDC on March 8, 2007. Given the amount of information and awareness of the potential expansion, we maintain our position that NYCIDA should have recaptured benefits from Baldor as stipulated in its lease agreement with NYCIDA.

RECOMMENDATIONS

We recommend that NYCIDA:

1. Ensure the project financial data received is sufficient and independently verified before a project is submitted for Board approval.

   NYCIDA Response: NYCIDA disagrees. "A Project's financial data is thoroughly reviewed when it is received by NYCIDA staff. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

   Auditor Comment: Entities such as consultants, financial advisors, underwriters, etc. have a vested interest in obtaining City benefits. Accordingly, it is imprudent and inappropriate for NYCIDA officials to make decisions about the City's economic development solely on the basis of analyses performed by these parties. Accordingly, we continue to recommend that NYCIDA conduct its own independent analyses of project data to ensure that City benefits are granted only to those companies that will, in fact, create jobs and meet their overall financial obligations.

2. Perform an independent analysis of the applicant's ability to meet all equity and debt requirements associated with the project and to ensure projects meet the intended purposes, sustain the operations as proposed, and meet the employment expectations to justify all the benefits received.

   NYCIDA Response: "Significant financial analysis is performed prior to any project being presented to the NYCIDA Board of Directors by Agency staff as well as outside financial experts. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project."

   Auditor Comment: As previously stated, entities, including underwriters and placement agents, have a vested interest in obtaining City benefits. Accordingly, NYCIDA should conduct its own independent analyses of prospective applicants.

3. Monitor project compliance report submissions to ensure the projects comply with their job retention and creation requirements as established in the application.

   NYCIDA Response: "While NYCIDA Compliance is open to recommendations on how to improve upon its current internal procedures, NYCIDA feels its current procedures are adequate to monitor job retention and creation requirements."

Auditor Comment: Obviously, NYCIDA's current procedures were inadequate to ensure that all projects were compliant with their obligations to generate and retain the appropriate number of jobs.

4. Conduct adequate reviews of project data to ensure Sales Tax exemptions are appropriately claimed and accurately reported.

   NYCIDA Response: "While NYCIDA Compliance is open to recommendations on how to improve upon its current internal procedures, Compliance actively reviews project data and sales tax exemptions claimed in order to uncover any misuse of the sales tax benefits."

   Auditor Comment: Given that our audit results showed deficiencies in the use of sales tax exemptions, NYCIDA must take steps to ensure that exemptions are appropriately claimed and accurately reported.

5. Establish internal controls to avoid unauthorized use of Sale Tax Letters.

   NYCIDA Response: "The Agency believes that NYCIDA followed its current practices for monitoring the use of Sales Tax Letters and preventing their unauthorized use. We believe that, consistent with statewide practices our current policies and procedure adequately monitor the use of Sales Tax Letters."

   Auditor Comment: As stated above, deficiencies in the use of sales tax letters and exemptions belie NYCIDA's belief that its procedures are adequate for monitoring the use of Sales Tax Letters.

6. Conduct periodic site visits to verify project operations and compliance status.

   NYCIDA Response: "While NYCIDA agrees that periodic site visits are needed, NYCIDA Compliance conducts periodic site visits to verify project operations and compliance status. While we continue to strengthen our monitoring procedures, 44 were site visits performed in fiscal year 2009 (the audit period) and over 100 were performed in fiscal year 2011. We believe these results to be significantly better than those implied by the Audit Report and believe them to be robust."

   Auditor Comment: Notwithstanding NYCIDA's contention that its Compliance unit conducts periodic site visits, we noted that these visits were not conducted for all 42 sampled projects.

7. Enforce the recapture provisions of the project agreements to ensure City forgone revenue and employment benefits are not lost, and document its decision-making process and the specific criteria used to decide whether or not to enforce the recapture provisions of project agreements.

NYCIDA Response: "While NYCIDA actively pursues recapture where it is available as a remedy, the Agency also believes strongly in working with companies to maintain their presence, employees and operations within New York City. Consequently, prolonged negotiations and recapture scenarios sometimes do result. The Agency will consider ways to better document the decision-making criteria used during negotiation periods in order to better document benefit recapture and terminations."

Auditor Comment: We continue to recommend that regardless of how long it takes NYCIDA to officially terminate a project, NYCIDA should ensure that all benefits, including PILOTs, are recaptured from the time that a project is declared to be in default.

DETAILED SCOPE AND METHODOLOGY

We conducted this performance audit in accordance with generally accepted government auditing standards, except for organizational independence as disclosed in the following paragraph. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

We are issuing this modified GAGAS compliance statement because of the Comptroller's mandated non-audit responsibility regarding NYCIDA. The Comptroller is a member of the Board of Directors of NYCIDA. The Comptroller maintains this position pursuant to New York State General Municipal Law §917-d, which requires that the Comptroller, as the City's chief fiscal officer, be a member of the Board of Directors of NYCIDA. Accordingly, the bylaws of NYCIDA specify that the Comptroller be a member of the Board. The Comptroller participates on the Board of NYCIDA through a designee. The Comptroller's designee was not involved in planning or conducting this audit or in writing or reviewing the audit report.

The scope of this audit was all projects reported in NYCIDA's PARIS for Fiscal Year 2009 (July 1, 2008, through June 30, 2009). To obtain an understanding of NYCIDA's operations and internal control processes, we reviewed the annual management agreement between NYCEDC and NYCIDA; NYCIDA's powers and duties under the New York State General Municipal Law Article 18-A, applicable provisions of Local Law 48, and the Public Authority Accountability Act. In addition, we reviewed NYCIDA's certified financial statements, internal audit reports, organization charts, policies and procedures manual, and Board of Directors' minutes and the PARIS report.

To familiarize ourselves with NYCIDA's project evaluation and monitoring functions, we reviewed its operating procedures manual, project application process including required documentation, and compliance requirements. We also conducted walk-through meetings of the application and compliance areas and interviewed key NYCIDA officials and personnel. We documented our understanding of NYCIDA operations and internal control processes through written narratives and flowcharts.

To assess the reliability of the project information reported by NYCIDA, we conducted a walk-through of the Project Application Tracking System (PATS), an internal database managed by NYCIDA's Compliance Department, and its interface with PARIS. We also reviewed on a limited basis the project data generated by PATS and uploaded into PARIS. In addition, NYCIDA's Research Department also uses Regional Input-Output Modeling System (RIMS) analysis to quantify the economic and fiscal impact of the investment projects. We reviewed input and output of its RIMS analysis to determine the reliability of the data.

To determine whether NYCIDA properly reviewed and evaluated information for project approvals, we conducted an analytical review of all 576 projects (totaling PILOT payments of $345.7 million and tax exemptions of $497.3 million) reported in the PARIS report for 2009. Based on our review, we judgmentally selected a sample of 42 major projects with the highest amount of sales tax exemptions and lowest number of reported employment data (totaling PILOT payments of $143,116,815 and tax exemptions of $195,962,334). Because three of the application files were unavailable, we were only able to review 39 application files. For the 39 projects reviewed, we analyzed the application process in terms of the completeness of submitted documentation as required and the reasonableness and justification of the project approvals. Specifically, we examined the documents submitted by the applicants, including inducement letters, completed core application, financial statements, financing commitment letters, various required questionnaires, results of due diligence checks, executive summaries presented to the Board, and inducement resolutions for accuracy and completeness.

To determine whether NYCIDA properly monitored the project compliance with required quarterly and annual submissions, we analyzed the compliance files maintained for the same 42 sampled NYCIDA projects. We reviewed the related project and lease agreements and examined semi-annual certificate and annual certifications, insurance certificates, EBR, submissions, NYS-45 and ST-340 submissions, Project Property Registries, field visit reports, and other related correspondence. Specifically, to determine whether NYCIDA monitored the job retention requirements of its project agreements, we reviewed the base employment requirements for all 16 commercial projects (totaling PILOT payments of $133,844,396 and tax exemptions of $165,430,752) from our sample of 42 projects and compared the amounts to the employment reported in the projects' required annual certification submissions. Further, we traced the reported information from each project's submission to the 2009 PARIS report for accuracy and completeness.

The result of the above tests, in conjunction with our other audit procedures, while not projected to the respective population from which the samples were drawn, provided a reasonable basis to satisfy our audit objectives.

NYCEDC
New York City Economic Development Corporation

January 27, 2012

Ms. Tina Kim
Deputy Comptroller for Audits
The City of New York
Office of the Comptroller
1 Centre Street
New York, New York 10007-2341

Re: Audit Report on the New York City's Industrial Development Agency's Project Financing, Evaluation, and Monitoring Process FN11-054A

Dear Ms. Kim:

Thank you for the opportunity to respond to the above referenced Draft Audit Report, dated January 12th, 2012.

We have specifically addressed each finding and recommendation made in the Draft Audit Report. If you or members of your staff have any questions please feel free to contact Jonathan Gouveia, Executive Director, New York City IDA (212) 312-3531.

Very truly yours,

Kyle Kimball,
Chief Financial Officer
New York City Industrial Development Agency

Attachment

cc: Seth Pinsky
Jonathan Gouveia
Josh Wallack
David Ehrenberg
Howard Spieler
Hope Mallari
George Davis, Mayor's Office of Operations

Response to Audit Findings and Conclusions
Executive Summary

New York City Industrial Development Agency (the "Agency" or "NYCIDA") thanks the City of New York, Office of the Comptroller ("Comptroller") for the opportunity to respond to the January 12, 2012 draft audit report (the "Audit Report") on the NYCIDA. The Agency appreciates the recognition by the Comptroller of its compliance with the Public Authority Accountability Act requirements and PARIS reporting. The Agency also appreciates the general recognition by the Comptroller of the depth of the work of the NYCIDA and its staff.

The findings described in the Audit Report can be grouped into three categories. The Agency respectfully disagrees with the findings of the Audit Report and offers three general responses, followed by specific statements in response to each of the findings.

Agency Staff and Outside Experts Conduct Significant Financial and Other Due Diligence Prior To Presenting Any Project to the NYCIDA Board of Directors
The Comptroller's first general finding is that the Agency fails to ensure that projects are financially feasible. However, the Agency consistently collects, reviews and analyzes audited financial statements, federal tax returns and a variety of other financial and business documentation. In addition to its own due diligence, as a conduit issuer, NYCIDA relies on technical expertise provided by underwriters, placement agents, third-party advisors and bond purchasers. Through its own analysis and the work of these outside experts, significant diligence is performed on every project to ensure that it is financially viable prior to seeking approval from the Board of Directors to grant benefits. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project.

The Agency Rigorously Monitors all Existing Projects. The Agency's Monitoring Policies Were Recently Cited as a Model for Other IDAs by a Watchdog Organization
The Comptroller's second general critique is that the Agency fails to monitor existing projects to ensure compliance. However, the Agency actively monitors the over 500 active projects for compliance. Indeed, 97% of NYCIDA's projects are compliant with their agreements and current on their obligations. While we believe our monitoring processes to be robust, the Agency continually attempts to strengthen its internal processes, and has taken additional steps since 2009. Good Jobs New York, a watchdog organization, recently cited NYCIDA's compliance efforts as a model for IDAs throughout the State of New York.

The Agency Aggressively Pursues its Legal Remedies When Projects Fail to Meet Their Obligations. These NYCIDA Policies Too Were Recently Cited as a Model for Other IDAs
The Comptroller's third general critique is that the Agency fails to terminate projects that are in default and to recapture benefits where appropriate. NYCIDA's projects overwhelmingly succeed. However, when projects fail to meet their obligations and the NYCIDA has a legal claim to recapture, the Agency aggressively pursues such repayments. Indeed, since 2002 the NYCIDA has recovered over $85 million in benefits and defaulted over 105 projects due to non-compliance. Good Jobs New York also recently praised NYCIDA's efforts around transparency and recapture as a model for other IDAs throughout the State of New York.

Full Response to Audit Findings and Conclusions

Comptroller Audit Finding #1: Inadequate Review and Evaluation of Project Information

a. *Inadequate Review and Evaluation of Project Information*

NYCIDA Response:

The Agency disagrees with the finding that Agency staff do not sufficiently review and evaluate project information. Specifically, the Audit Report cites the opening sentence of Section 2.D of the NYCIDA Project Manager Checklist that states that staff should perform "independent analysis of the applicant's ability to meet all equity and debt requirements associated with the project". The report concludes that Agency staff do not meet this standard. However, the Audit Report neglected to acknowledge that the above referenced statement was a subtitle to a paragraph that immediately follows, which provides a precise description of the type of analyses contemplated in this section. The checklist specifically states that project managers should collect and analyze audited financial statements or tax returns if audited financial statements are unavailable, request projections to clarify applicants' financing plans and analyze this data using standard NYCIDA financial models. Project managers consistently complete the steps contemplated in this section of the checklist in advance of presenting projects to the NYCIDA's Board of Directors.

It is worth noting that the Agency collects an extensive list of project and supporting data in order to conduct a cost-benefit analysis and analyze the environmental impacts of a proposed action, in each case, as required by statute. Furthermore, for each project Agency staff conducts additional due diligence, including confirming financing commitments, reviewing the background and experience of the applicant and its principals and assessing the reasonableness of financial projections. The list of data and supporting documents collected and reviewed includes:

1. Three years of company financials or tax returns
2. Four quarters of NYS-45s
3. Sources and uses of project funds
4. Contract of sale or lease related to project
5. Project description and information on how the project relates to current operations
6. Financing contracts and/or commitments
7. Summary of company background, including company history and lists of affiliated unions, labor issues, suppliers, customers, funding sources and banks
8. Payroll of existing companies
9. Resumes of company principals
10. Current employment and post-project employment projections and wage data
11. Internal Background Investigation Questionnaire
12. Doing Business Data Form
13. Environmental reports

Finaly, while Agency staff perform significant due diligence prior to bringing items to the Board, the NYCIDA is a conduit bond issuer *not* a financial advisor nor an underwriter. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project.

b. *Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc.*

NYCIDA Response

The Audit Report states that the NYCIDA: 1) did not properly assess the performance of Wartburg Nursing Home, Inc.; 2) justified its decision based on ongoing capital investments at the existing facility that did not occur; and 3) ignored changes to Medicare and Medicaid reimbursements. These findings are factually incorrect. First, in accordance with the Agency's UTEP, the Agency collected all relevant financial and other supporting data to conduct the reviews described in the prior response. In addition, in reviewing the project, the Agency considered the financial strength of both Wartburg Lutheran Nursing Home for the Aging and Wartburg Nursing Home, Inc. (an affiliate of the borrowing company). Second, negative cash flows were analyzed by NYCIDA staff but were, in part, explained by a large and non-recurring renovation to their facility. The Audit Report's statement that no evidence existed in Wartburg's audited financials as to this investment is incorrect as Wartburg's financial statements indicated that the organization's fixed assets increased by over $1mm during the period between 2003 and 2004 due to the renovations/improvements. Additional increases in net assets would have appeared on the statements but were offset by depreciation during the same period. Third, the Agency did not ignore changes to Medicare and Medicaid reimbursements and disclosed such changes in the materials provided to the Board of Directors.

Finally, it is important to note that technical underwriting and due diligence expertise was provided by First Albany Capital, that served as Underwriter, and Amalgamated Bank, which provided a Letter of Credit. Again, the Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project.

c. *Bronx Parking*

NYCIDA Response:

The Agency disagrees with the finding that NYCIDA did not ensure that its staff gathered sufficient information to allow it to make a well-informed recommendation. The Bronx Parking Development Company project was financed following the completion of an extensive independent third-party parking system feasibility analysis, conducted by Desman Associates, a nationally recognized expert in that field. The study included a "review and analysis of the current and projected demand for parking in the vicinity of the Yankee Stadium, the multi-year parking revenue projections, the operation/maintenance budget and the long-term capital repair and replacement expense budget" (Desman Report, Page 1) for the project. This study was included, with the consent of Desman, in the Official Statement presented to prospective bond purchasers. In addition, contrary to findings in the Audit, the Agency did analyze and adopt findings under the State Environmental Quality Review Act which specifically addressed the issue of a reduction in required parking spaces needed for the project as the result of the construction of a new MetroNorth commuter rail station adjacent to the new Yankee Stadium.

This reduction in parking spaces was also reflected in the independent feasibility analysis completed by Desman. Again, the Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project.

d. *Hollow Metal Factory Outlet Corp*

NYCIDA Response:

The Agency disagrees with the assertion that the projected profits and resulting corporate taxes were too minimal to justify NYCIDA's decision to grant tax benefits. The company's projected tax liabilities such as corporate and payroll taxes are not the only factor used to determine a project's validity. The standard cost-benefit analysis, which is one component of the analysis performed as part of all project reviews, takes into account a wide range of fiscal impacts to determine if tax incentives should be provided. A full cost benefit analysis was performed, using the industry standard model, and showed a positive return to the City from the proposed project.

Comptroller Audit Finding #2: Inadequate Project Monitoring

a. *Employment Levels Not Achieved*

NYCIDA Response:

The Agency disagrees with the assertion that NYCIDA should review the threshold percentage allowed to each commercial project in order to encourage companies to maintain a more desirable employment level. The employment threshold percentages are established in Project Agreements to account for general fluctuations in employment levels that are part of a company's usual course of business. As documented in the Project Agrements, significant employment declines may be cause for termination or recapture. However, more minor and/or cyclical fluctuations do not necessarily trigger such penalties. As became evident in 2008, employment declines for many companies were an unavoidable result of a global economic recession. We believe the thresholds established in the Project Agreements strike a fair balance between ensuring the City realizes the employment benefits it anticipates while not penalizing companies for employment changes that are a normal part of running a business. Where applicable, the NYCIDA Compliance Department ("Compliance") enforced available remedies with respect to the projects listed in the table in the Audit Report that fell below their employment thresholds. The result was a termination of benefits and/or project documents.

- Bear Stearns: Benefits and Project Agreement terminated
- Depository Trust Company: Penalties are not applicable
- Information Builders: Benefits and Project Agreement terminated
- Merrill Lynch: Benefits and Project Agreement terminated
- Time: Benefits and Project Agreement terminated
- Viacom: Benefits and Project Agreement terminated
- VNU: Benefits terminated

b. *Did Not Adequately Monitor to Ensure Job Retention Requirements Were Met*

NYCIDA Response:

The Agency disagrees with the finding that the NYCIDA did not adequately monitor project compliance with job requirements. The audit states that of the 42 projects sampled, six (or 14.3%) did not submit an Employment and Benefit Report (EBR). However, five of those six projects were terminated during FY2009. Companies are not required to submit their annual EBR if they no longer have an active agreement with NYCIDA at the end of the fiscal year.

- Hollow Metal Factory Outlet Corp terminated on March 17, 2009 and did not have an active agreement at the end of FY2009
- Wartburg Lutheran Nursing Home for the Aging terminated on September 9, 2008 and did not have an active agreement at the end of FY2009
- Paradise Products Corp. terminated on May 7, 2009 and did not have an active agreement at the end of FY2009
- Viacom, Inc. terminated on April 30, 2009 and did not have an active agreement at the end of FY2009
- St. Bernard's School terminated on July 15, 2008 and did not have an active agreement at the end of FY2009

NYCIDA compliance staff actively pursued the one remaining EBR, but was unable to secure it from the project company. However, Compliance was able to confirm that the company was meeting its obligations under the Project Agreements without the EBR, so the lack of this one form had no material impact on benefits granted or termination/recapture thereof.

The project files that were selected for review during the audit only represents a sample of the entire portfolio of active projects Compliance currently monitors. Indeed, in FY2009, 97% of all active NYCIDA projects submitted EBRs. Excluding projects that were in default, terminated or eventually terminated 99% were collected. In FY2011, Compliance collected 99% of all EBRs from our active portfolio. Excluding projects that were in default, terminated or eventually terminated, 100% were collected.

Additionally, the Quarterly Combined Withholding, Wage Reporting, And Unemployment Insurance Return form (the "NYS-45") is required to be submitted to NYCIDA by project companies along with the employment report. Where applicable, the NYS-45 is used by Compliance to verify reported employment of companies. However, because the NYS-45 includes employees at all corporate locations within the State, it is not an effective compliance tool for companies that have locations outside the City or additional locations within the City that are not the subject of the benefit agreement. In such cases, Compliance uses other available methods and submissions to verify employment levels at the project location.

c. *NYCIDA Lacks Controls over the Use of Sales Tax Letters*

NYCIDA Response:

The Agency disagrees with the finding that NYCIDA lacks controls over the use of sales tax letters. NYCIDA works in close collaboration with New York State Department of Taxation and Finance ("NYSDOTF") to administer sales tax letters in accordance with general practice and sales tax exemption procedures. All NYCIDA sales tax letters are reviewed and renewed annually and have a clear expiration date. Each letter also provides details of eligible purchases and locations. When the letter expires, is cancelled due to non-compliance, or if benefits are terminated before the letter's expiration date, Compliance requests that the original letter be returned.

In the event of unauthorized use by a project company, NYCIDA, in conjunction with the NYSDOTF, pursues corrective action, which typically results in repayment of benefits and/or interest and penalty, if applicable. Furthermore, project companies, their contractors and their vendors are subject to audit by NYSDOTF.

In addition to the above controls for use of sales tax letters, all projects with an active sales tax letter are required to file an ST-340 form with NYSDOTF (with a copy to NYCIDA) detailing the exemptions claimed in a given calendar year. These are aggressively collected and monitored by Compliance in addition to NYSDOTF. For calendar year 2010, the most recent date the form was due to the State, 96% of all projects sent copies to the Agency.

Finally, the Agency's Commercial Growth projects are required to submit a detailed registry for all purchases made utilizing the sales tax letter. These are carefully reviewed by Compliance to verify project purchase eligibility and benefit usage. In addition, most commercial growth projects are required to submit tri-annual reviews of their purchases performed by certified public accountants and are always subject to audit by NYSDOTF should one be requested.

d. *Did Not Conduct Periodic Project Site Visits*

NYCIDA Response:

The Agency disagrees with the finding that periodic site visits are not performed to NYCIDA project locations to authenticate employment and capital investments. It is true that of the 42 projects the Comptroller's Office sampled, a very small number received site visits in FY 2009. However, the selected sample simply is not representative of the Agency's oversight of its entire portfolio of projects, either in FY2009 or in subsequent years. Compliance conducted 44 site visits in FY2009, 75 in FY2010, and 119 in FY2011.

Starting in FY2012, Compliance commenced a five-year self-audit plan in which 20% of the portfolio (about 105 projects as of FY2012) will be thoroughly reviewed each year, including, but not limited to, an on-site field visit inspection. In combination with our pre-existing site visit policies the Agency expects to, and are indeed on pace to, perform significantly more site visits than the 120 performed last year.

Another example of the Agency's continued effort to strengthen its compliance efforts occurred in the Spring 2011 when Compliance collaborated with the NYC Law Department to further develop best practices for performing site visits and drafting site visit reports.

NYCIDA continues to increase its compliance activity and make our existing processes more effective. The Agency agrees that monitoring and site visits are critical to ensuring that the City gains the employment benefits it expects from NYCIDA projects. However, the Agency does not believe that the sample cited by the Comptroller was representative of its monitoring efforts, either in FY2009 or in subsequent years.

Comptroller Audit Finding #3: NYCIDA Did Not Initiate the Benefits Recapture Process and Ensure that Projects Were Terminated in a Timely Manner, Resulting in at Least a $16,184,760 Loss in City and Other Benefits

a. *$14,374,960 in Forgone Benefits Recapture Due to Project Non-Compliance*

NYCIDA Response:

The Agency disagrees with the assertion that NYCIDA improperly allowed tax and energy benefits for Fiscal Year 2009. On November 1, 1989, Chase Manhattan Bank (successor in interest to JPMorgan Chase & Co.) entered into a commercial incentive bond transaction with NYCIDA to acquire and maintain designated facilities in what is now known as Brooklyn's MetroTech Center. On September 1, 1999, The Bear Stearns Companies Inc. entered into a commercial incentive straight-lease transaction with NYCIDA to maintain at least 5,700 employees in New York City through 2049 in return for energy benefits, real property tax benefits and sales tax benefits.

In 2008, in response to an economic downturn, Bear Stearns signed a merger agreement with JP Morgan Chase ("JPMC"). Thereafter, NYCIDA Compliance sent a letter to JPMC asking that they report the details of the merger to the Agency, in accordance with the Project Agreement. Negotiations with JPMC occurred between August 2008 and January 2009 about potential restructuring options for the transaction.

Under both the IDA Project Agreement and the NYCPUS Power Service Agreement, JPMC, as the successor to Bear Stearns, was entitled to continue to receive energy benefits, real property tax benefits and sales tax benefits. After negotiations with the NYCIDA, in August 2010, JP Morgan Chase agreed to terminate the NYCIDA Project documents, notwithstanding that a substantial amount in unused sales tax benefits remained available to JPMC under the agreement. In addition, although termination documents were not executed until 2011, JPMC agreed that NYCPUS energy benefits would cease on October 28, 2010. Under the Project Documents, the Agency was not entitled to demand a recapture of benefits based on the reduction in the number of Bear Stearns employees following the Chase's acquisition of Bear Stearns.

It is also important to note that JPMC's obligations (i) to continue reporting the number of Bear Stearns employees employed by it and (ii) to maintain the headquarters of Bear Stearns Companies LLC, a subsidiary of JP Morgan Chase, in New York City, survived the termination of the Project Agreements and remain in effect. NYCIDA also continues to have benefits recapture rights that may be exercised if JPMorgan Chase relocates Bear Stearns employees or the Bear Stearns headquarters outside of New York City.

b. *Did Not Recapture $520,800 Due to Early Termination*

NYCIDA Response:

The Agency disagrees with the finding that the Agency was required to initiate a benefit recapture action. The Agency did not make a recapture claim against Wartburg Lutheran Home for the Aging and Wartburg Nursing Home, Inc. (the "Borrower") as the Borrower entered into a Voluntary Receivership Agreement pursuant to Section 2810 of the Public Health Law with the Department of Health. The purpose of Section 2810 is to provide a bankruptcy-type procedure for facilities like the Borrower's not-for-profit nursing home; and the purpose of the procedure is to insure the safety and continued servicing of a needy population.

In connection with that agreement, the Borrower was under contract to sell its realty and its assets to, respectively, Wartburg Realty LLC and Wartburg Receiver LLC. While the Agency's recapture provisions in the Borrower's agreements with the Agency literally apply to a "sale" of the project facility, the sale that in fact occurred arose out of distressed circumstances pursuant to a statutory procedure designed to protect a vulnerable population, service continued to be provided to this population and the jobs that the Agency's assistance sought to create continued. It was the Agency's determination that pursuing recapture in such a circumstance did not further the policy objective underlying the original transaction.

Furthermore, the Wartburg Nursing Home has continued to operate as a full service nursing home at the project location.

c. *Improperly Allowed $79,000 in City PILOT Benefits Due to Delay in Termination*
d. *Improperly Allowed $50,000 in City PILOT to a Defaulted Project*

<u>NYCIDA Response</u>:

The Agency disagrees with the finding that NYCIDA improperly continued City PILOT benefits to Paradise Products Corp. and Austin Automotive Warehouse Corp. In general NYCIDA strives to expedite benefit suspension and/or terminations to ensure projects are placed back on City tax rolls and incentives cease to accumulate. NYCIDA expeditiously pursues recapture as applicable and appropriate under the Project Documents.

The Agency also takes the task of supporting businesses and maintaining employment in the City very seriously, and as a result, pursues not only the penalties available under the Project Documents, but also seeks to negotiate with companies in an attempt to preserve jobs and best serve the City as whole. In the aforementioned examples, the Agency ultimately terminated project documents but only after all available options were exhausted for the projects to maintain operations and provide the greatest benefit to the City.

a. *Improperly Waived $1.16 Million in City Tax and Other Benefits Recapture*

<u>NYCIDA Response:</u>

The Agency disagrees with the finding that NYCIDA improperly waived a recapture of benefits from Baldor Specialty Foods Inc. Baldor outgrew the project facility and was seeking a new location in order to expand its operations and employment. The Company evaluated its options for relocation and concluded that another facility in the Bronx would best serve their needs during expansion. The Company's relocation from its designated project location did technically constitute a recapture event under their Project Agreements. However, given that they were relocating and indeed expanding within the City, it did not serve NYCIDA's policy objective to terminate and recapture benefits of a company that was increasing its commitment to the City. Additionally, under current NYCIDA Board-approved UTEP guidelines this would no longer be a recapture event under the documents (provided they maintain similar employment at the new location).

The Company has since made significant investments in the new facility while growing its employment from 517 employees in 2007 (original location) to 556 employees in 2009 (new facility), an increase of seven percent.

Response to Comptroller Audit Recommendations

For the reasons outlined herein, the Agency generally does not agree with the recommendations made in the Comptroller's Audit Report. However, the Agency remains committed to strengthening its policies and practices wherever possible and looks forward to working with the Comptroller's office and its designee on the NYCIDA Board in the future.

Recommendation #1: "Ensure the project financial data received is sufficient and independently verified before a project is submitted for Board approval."

NYCIDA Response: We disagree with the recommendation that a project's financial data should be reviewed by an independent evaluator. A Project's financial data is thoroughly reviewed when it is received by NYCIDA staff. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project. The Agency believes that its current policies and procedures strike the right balance between performing internal reviews of project financial information while not crossing the important line between the Agency as a conduit issuer and the financial experts who play important roles in these transactions.

Recommendation #2: "Perform an independent analysis of the applicant's ability to meet all equity and debt requirements associated with the project and to ensure projects meet the intended purposes, sustain the operations as proposed, and meet the employment expectations to justify all the benefits received."

NYCIDA Response: Significant financial analysis is perfomed prior to any project being presented to the NYCIDA Board of Directors by Agency staff as well as outside financial experts. The Agency and its legal counsel believe that, as a conduit issuer, it would be inappropriate for Agency staff to usurp the role of the professional, expert consultants, financial advisors, underwriters, placement agents and borrowers who together produce the materials upon which lenders or bond investors make a determination as to the financial viability of a particular project. The Agency believes that its current policies and procedures strike the right balance between performing internal reviews of project financial information while not crossing the important line between the Agency as a conduit issuer and the financial experts who play important roles in these transactions.

Recommendation #3: "Monitor project compliance report submissions to ensure the projects comply with their job retention and creation requirements as established in the application."

NYCIDA Response: While NYCIDA Compliance is open to recommendations on how to improve upon its current internal procedures, NYCIDA feels its current procedures are adequate to monitor job retention and creation requirements. As has been normal course and as we believe was the case during the entire audit period, NYCIDA currently monitors project compliance with job retention and creation requirements, and enforces remedies when applicable.

Recommendation #4: "Conduct adequate reviews of project data to ensure Sales Tax exemptions are appropriately claimed and accurately reported."

NYCIDA Response: While NYCIDA Compliance is open to recommendations on how to improve upon its current internal procedures, Compliance actively reviews project data and sales tax exemptions claimed in order to uncover any misuse of the sales tax benefits. The Agency enforces remedies and/or penalties when a misuse or an unauthorized use of the benefit occurs.

Recommendation #5: "Establish internal controls to avoid unauthorized use of Sale Tax Letters."

The Agency believes that NYCIDA followed its current practices for monitoring the use of Sales Tax Letters and preventing their unauthorized use. We believe that, consistent with statewide practices our current policies and procedure adequately monitor the use of Sales Tax Letters

Recommendation #6: "Conduct periodic site visits to verify project operations and compliance status."

NYCIDA Response: While NYCIDA agrees that periodic site visits are needed, NYCIDA Compliance conducts periodic site visits to verify project operations and compliance status. While we continue to strengthen our monitoring procedures, 44 were site visits performed in fiscal year 2009 (the audit period) and over 100 were performed in fiscal year 2011. We believe these results to be significantly better than those implied by the Audit Report and believe them to be robust.

Recommendation #7: "Enforce the recapture provisions of the project agreements to ensure City forgone revenue and employment benefits are not lost, and document its decision-making process and the specific criteria used to decide whether or not to enforce the recapture provisions of project agreements."

NYCIDA Response: While NYCIDA actively pursues recapture where it is available as a remedy, the Agency also believes strongly in working with companies to maintain their presence, employees and operations within New York City. Consequently, prolonged negotiations and recapture scenarios sometimes do result. The Agency will consider ways to better document the decision-making criteria used during negotiation periods in order to better document benefit recapture and terminations.