



# City of Rochester, NY

## Community Development Block Grant Program

**Office of Audit, Region 2  
New York - New Jersey**

**Audit Report Number: 2016-NY-1003  
February 5, 2016**

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**To:** William T. O'Connell, Director, Community Planning and Development  
Division, Buffalo, NY, 2CD

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**From:** Kimberly Greene, Regional Inspector General for Audit, 2AGA

**Subject:** The City of Rochester, NY, Did Not Always Administer Its Community  
Development Block Grant Program in Accordance With HUD Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the City of Rochester, NY's Community Development Block Grant program.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 212-542-7984.



**Audit Report Number: 2016-NY-1003**

**Date: February 5, 2016**

**The City of Rochester, NY, Did Not Always Administer Its Community Development Block Grant Program in Accordance With HUD Requirements**

## Highlights

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### What We Audited and Why

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We audited the City of Rochester's Community Development Block Grant (CDBG) program to address our audit plan priority to improve financial management controls over CDBG grants. We selected this grantee based on a risk analysis of grantees administered by the U.S. Department of Housing and Urban Development's (HUD) Buffalo field office, which considered funds received and the risk score assigned by HUD. The City received more than \$32.7 million in CDBG funds in program years 2011 through 2014. The audit objective was to determine whether City officials established and implemented adequate controls to ensure that the CDBG program was administered in accordance with applicable requirements.

### What We Found

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City officials had not established and implemented adequate controls to ensure that CDBG funds were always administered in accordance with applicable requirements. Specifically, they did not always spend CDBG funds for eligible and supported costs, draw down and disburse Section 108 loan funds in a timely manner, make adequate efforts to collect a delinquent float loan, execute a procurement in compliance with Federal procurement regulations, and adequately monitor subrecipients. As a result, the City spent \$153,279 and more than \$8.1 million for ineligible and unsupported costs, respectively, and did not ensure that \$1.5 million was spent for its intended use.

### What We Recommend

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We recommend that the Director of HUD's Buffalo Office of Community Planning and Development instruct City officials to (1) reimburse from non-Federal funds the \$153,279 spent for ineligible costs, (2) provide documentation for the eligibility of \$291,236 in unsupported costs, (3) justify the untimely drawdown and disbursement of more than \$6.7 million of Section 108 loan funds, (4) reimburse the \$1.5 million disbursed for a delinquent float loan through one of the options identified in HUD regulations, (5) support that a \$1.2 million contract was fair and reasonable and that the sole-source method was appropriate, (6) develop and implement controls and comprehensive procedures to ensure the proper administration of the CDBG program, and (7) request CDBG program training from the HUD Office of Community Planning and Development field office.

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# Background and Objective

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The Community Development Block Grant (CDBG) program is authorized under Title 1 of the Housing and Community Development Act of 1974, Public Law 93-383, as amended, 42 U.S.C. (United States Code) 5301 et seq. The program provides annual grants on a formula basis to entitled cities and counties to develop viable urban communities by providing decent housing and a suitable living environment and expanding economic opportunities, principally for low- and moderate-income persons. To be eligible for funding, every CDBG-funded activity must meet one of the program's three national objectives: (1) benefit low- and moderate-income persons, (2) aid in preventing or eliminating slums or blight, or (3) address a need with a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community.

The City of Rochester, NY, is a CDBG entitlement grantee. The City operates under a mayor-council form of government, and its CDBG activities are administered through the Department of Neighborhood and Business Development, Office of the Commissioner. During program years 2011 through 2014, the U.S. Department of Housing and Urban Development (HUD) annually awarded the City more than \$7.5 million in CDBG entitlement funds, and it reported approximately \$3.8 million in CDBG program income during this period.<sup>1</sup> The City used its CDBG funds for various activities during this period, including housing rehabilitation, economic development, public facilities and improvements, public services, clearance and demolition, and program administration.

The objective of the audit was to determine whether City officials established and implemented adequate controls to ensure that the CDBG program was administered in accordance with applicable requirements. Specifically, we wanted to determine whether officials (1) established and implemented the necessary controls to ensure that program activities were adequately documented and administered in accordance with HUD regulations, (2) spent CDBG funds for eligible activities, (3) performed adequate monitoring of subrecipient administered activities, and (4) properly recorded program income receipts and expenditures.

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<sup>1</sup> The City's CDBG program year is July 1 through June 30.

# Results of Audit

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## **Finding: The City Had Control Weaknesses in Administering Its CDBG Program**

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City officials had not established and implemented adequate controls to ensure that CDBG funds were always administered in accordance with applicable requirements. Specifically, they did not always spend CDBG funds for eligible and supported costs, draw down and disburse Section 108 loan funds in a timely manner, make adequate efforts to collect a delinquent float loan<sup>2</sup>, execute a procurement in compliance with Federal procurement regulations, and adequately monitor subrecipients. We attributed these deficiencies to weaknesses in accounting for disbursements, City officials' unfamiliarity with HUD regulations, and inadequate subrecipient monitoring procedures. As a result, the City spent \$153,279 and more than \$8.1 million for ineligible and unsupported costs, respectively, and did not ensure that \$1.5 million was spent for its intended use.

### **Funds Disbursed for Ineligible Costs**

City officials disbursed \$153,279 in CDBG funds for ineligible costs. They awarded a borrower a \$1 million loan for planning and administrative soft costs related to the purchase and redevelopment of a City-owned building. Later, they drew down \$99,616 to reimburse the borrower for costs incurred before this activity was included in the City's amendment to its 2010-2011 annual action plan and for duplicate payments claimed by the borrower. Regulations at 24 CFR (Code of Federal Regulations) 570.200(h) provide that a grantee may reimburse a recipient for costs incurred before the effective date of a grant agreement if the activity for which the costs were incurred was included in a consolidated plan action plan, an amended consolidated plan action plan, or an application under subpart M, Loan Guarantees, before the costs were incurred.

City officials also charged the City's CDBG program for salaries related to non-federally funded activities. During the first and second quarters of program year 2013, the salaries of three City employees were charged entirely to the CDBG economic development activity. Also, these three employees certified that they worked entirely on this activity. However, certified timesheets showed that a significant number of hours were charged to a non-Federal category. As a result, the City disbursed \$46,324 in CDBG funds to reimburse non-Federal salaries; thus, these costs were ineligible.

City officials also reimbursed duplicate costs to the subrecipient administering the foreclosure prevention program. Regulations at 2 CFR Part 225, appendix A, paragraph (C)(1)(a), provide

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<sup>2</sup> 24 CFR 570.301(b) defines float-funded activities as those carried out with funds borrowed from a grantee's CDBG program that are budgeted for other activities but not needed immediately and thus, undisbursed, and which can be repaid using the related program income.

that to be allowable under Federal awards, costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards. City officials used a subrecipient to conduct client intake and assessment, including gathering and analyzing household and financial information, foreclosure prevention through working with the client and mortgage lender, and outreach or promotion of the program. The subrecipient submitted 10 payment requests for \$335,000, of which 23 invoices totaling \$7,339 were duplicates. In addition, documentation for other invoices in support of disbursements was unorganized and did not clearly identify the amounts claimed. Regulations at 24 CFR 85.20(b)(2) provide that grantees and subgrantees must maintain records that adequately identify the source and application of funds provided for financially assisted activities. We attributed these deficiencies to weaknesses in accounting for disbursements.

### **Funds Disbursed for Inadequately Supported Costs**

City officials reimbursed a subrecipient administering the foreclosure prevention program \$291,236 in inadequately supported costs. While the majority of the costs for which the subrecipient claimed reimbursement were for salaries, the City's files did not include certifications or timesheets for the employees to ensure that the hours charged were eligible under the CDBG program. Regulations at 2 CFR Part 225, appendix B, require that certifications or timesheets be provided and signed by the respective employee. Therefore, the \$231,660 in salary costs reimbursed to the subrecipient was unsupported. In addition, \$12,253 was reimbursed without check copies, invoices, or receipts providing the necessary detail to ensure eligibility and reasonableness. Further, while City officials drew down \$335,000 to reimburse this subrecipient, the City's records disclosed that the subrecipient had submitted only \$287,677 in costs to be reimbursed by the City for a difference of \$47,323. We attributed these deficiencies to weaknesses in accounting for disbursements and inadequate monitoring. As a result, HUD lacked assurance that the \$291,236 (\$231,660 + \$12,253 + \$47,323) disbursed without adequate documentation was for eligible foreclosure prevention program costs.

City officials also disbursed \$221,810 for a loan related to the purchase and redevelopment of a City-owned building without sufficient documentation showing that costs were eligible and reasonable. For example, 24 expenditures lacked invoices, and 18 lacked copies of checks as required to support that the borrower had incurred the expenses. Regulations at 24 CFR 85.20(b)(2) require that grantees and subgrantees maintain records that adequately identify the source and application of funds provided for financially assisted activities. The promissory note executed between the City and the borrower on December 20, 2013, provided that the City would disburse the loan proceeds upon submission of invoices, receipts, and other documentary proof, including but not limited to copies of the front and back of cancelled checks, such proof to be satisfactory to the City, evidencing the redevelopment costs which were to be reimbursed from proceeds of the loan. As a result of our review, City officials followed up with the borrower to obtain additional documentation to support that the \$221,810 was spent for eligible costs.

In addition, salary costs for City employees charged to the CDBG program were not always adequately supported or correctly reported. Reconciliation of the City's certified timesheets and Accounting Department calculations for program year 2013 salaries reimbursed under the

CDBG-funded rehabilitation activity disclosed multiple inconsistencies, such as addition errors, entry errors, missing timesheets, and timesheets that did not include the signature of the employee or his or her supervisor. Regulations at 2 CFR Part 225, appendix B, require that personnel activity reports be signed by the employee, and City procedures required supervisory certification. Four of the timesheets submitted during the fourth quarter of program year 2013 were missing the employee's signature and included \$7,112 in CDBG funding. In addition, while City officials reported in HUD's Integrated Disbursement and Information System<sup>3</sup> (IDIS) that they spent \$2.1 million for this rehabilitation administration activity in program year 2013, City records showed that the costs were related to general CDBG staff costs, including City salaries for economic development, demolition, and housing development activities, in addition to rehabilitation. We attributed these deficiencies to weaknesses in accounting for disbursements. There was no monetary effect upon the amount of CDBG funds drawn down because the City incurred more CDBG-eligible salary costs in the third and fourth quarters of program year 2013 than it drew down. However, the incorrect categorization of these expenditures resulted in inaccurate reporting to HUD regarding how the City used its CDBG funding.

#### **Section 108 Loan Funds Not Drawn Down and Disbursed in a Timely Manner nor Accurately Reported**

City officials did not draw down and disburse Section 108 loan funds in a timely manner as required. Regulations at 24 CFR 570.705(b)(1) require that to ensure the repayment of debt obligations and the charges incurred and as a condition for receiving loan guarantee assistance, the recipient must execute a contract with HUD for loan guarantee assistance, which includes provisions for the repayment of debt obligations guaranteed. HUD awarded the City a \$20 million Section 108 loan in September 2012 for construction and permanent financing for phase one of the development of a mixed-use facility. The loan agreement between HUD and the City required that all funds in the guaranteed loan funds account or the guaranteed loan funds investment account be disbursed for approved activities by February 28, 2015, and that any funds remaining after that date be transferred to the loan repayment account for use in paying interest, principal, or other financial obligations or be temporarily invested until final payment and discharge of the loan indebtedness. However, City officials did not transfer any remaining funds as required, but rather, drew down a final withdrawal of \$6.7 million on March 25, 2015, which was not disbursed and deposited until April 1, 2015. While City officials requested an extension of the disbursement deadline from HUD on March 25, 2015, before making the \$6.7 million withdrawal, they were unable to document that HUD approved an extension. After our inquiry, City officials followed up with HUD and obtained written approval, dated June 2, 2015, for the extension. Consequently, while HUD's approval for the disbursement was granted more than two months after the date of the withdrawal, the City now has assurance that the funds were used for their intended purpose.

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<sup>3</sup> The Integrated Disbursement and Information System is the drawdown and reporting system for all of HUD's community planning and development formula grant programs.



In addition, although these funds were received by the City on April 1, 2015, they were not disbursed to the developer until more than 4 months later on August 17, 2015, after we inquired about their status. Regulations at 24 CFR 85.21(b) provide that the methods and procedures for payment should minimize the time between the transfer of funds and disbursement by the grantee. However, these funds were drawn down unnecessarily and not disbursed in a timely manner. We attributed these conditions to City officials' unfamiliarity with the contract provisions and HUD regulations pertaining to the withdrawal and disbursement deadlines.

Further, City officials' reporting on this loan in IDIS contained multiple inconsistencies. Four drawdowns totaling more than \$9.8 million that were reported in IDIS and disbursed maintained a status of "Pending HQ Approval." City officials stated that the wiring of the funds was not dependent on IDIS and, thus, HUD had wired all \$20 million of the funds, although these transactions were still identified as pending and requiring approval in the system. As a result of our inquiry, City officials contacted HUD's Office of Block Grant Assistance, Financial Management Division, to request retroactive approval of these vouchers in IDIS, which was granted in June 2015. In addition, City officials incorrectly entered the national objective for this loan as low- and moderate-income job creation or retention, which should have been entered as low- and moderate-income job creation, location based. The low- and moderate-income job creation or retention objective requires that at least 51 percent of the jobs created or retained involve the employment of low- and moderate-income persons, whereas the low- and moderate-income job creation, location based, objective is based on the poverty rates for the location of the project. We attributed this deficiency to an oversight on the part of City officials. After learning of this error, City officials made the necessary correction in IDIS.

#### **The City's CDBG Float Loans Inadequately Administered and Reported On**

City officials did not adequately publicize action to document the City's procedures for collecting amounts due on CDBG float loans or take action to collect on delinquent loans in a timely manner. They did not publicize in their annual action plans the float-funded activities and the City's commitment to undertake one of the options required by HUD regulations if the funds could not be repaid.

Regulations at 24 CFR 570.301 provide that grantees must note in their annual action plan what action they would take for delinquent float loans. The options for action include (1) amending or deleting activities in an amount equal to any default or the failure to show sufficient income in a timely manner, (2) obtaining an irrevocable line of credit from a commercial lender for the full amount of the float-funded activity, (3) transferring general local government funds in the full amount of any default or shortfall to the CDBG line of credit within 30 days of the float-funded activity's failure to generate the projected amount of the program income on schedule, or (4) obtaining HUD approval for securing a timely return of the amount of the float funding.

In addition, while two loans were repaid, a third loan for \$1.5 million had been delinquent more than 17 years. Regulations at 24 CFR 570.301 provide that the expected period between obligation of assistance for a float-funded activity and receipt of program income in an amount at least equal to the full amount drawn from the float to fund the activity may not exceed 2.5 years. An activity, from which program income sufficient to recover the full amount of the float

assistance is expected to be generated more than 2.5 years after obligation, may not be funded from the float. In 1992, City officials provided a \$1.5 million float loan and a \$4 million Section 108 loan to a borrower that defaulted in 1998. On September 19, 2012, the city council approved release of the lien for the unpaid \$1.5 million float loan, without HUD approval, so that the property could be sold to another developer. While, this developer agreed to assume a \$3.1 million note to assist the City in paying off the \$4 million Section 108 loan, it did not assume the \$1.5 million float loan. Thus, when the \$1.5 million float loan was still active and outstanding 24 years after its award, the City did not take any of the above mentioned steps required by the regulations at 24 CFR 570.301, and the \$1.5 million was unavailable for other eligible CDBG activity. Once we established that action was needed to collect the \$1.5 million delinquent debt, the City began efforts to identify any recoverable assets and declared its intention to request forgiveness from HUD.

City officials' reporting of their float loan activities in IDIS did not reconcile with supporting documentation maintained by the City. The CDBG float-funded activities report in IDIS showed that the City had not receipted payment on any of its CDBG float loans. However, the documentation maintained by the City for the two loans reviewed supported that it had received full repayment for them. According to HUD officials, the City did not enter any related activity for its receipts before 2009, which was optional at that time, and entered an incorrect activity for all receipts after 2009, resulting in its reporting inaccurate data to HUD for this period.

#### **Procurement Not Executed in Accordance With Federal Regulations**

City officials disbursed \$1.2 million under a contract to develop an open space area into an enhanced plaza that did not comply with Federal regulations. Regulations at 24 CFR 85.36 require that an invitation for bid be publicly advertised and solicited from an adequate number of known suppliers and that sufficient time be provided before the opening bid date. Additionally, for sealed bidding to be feasible, two or more responsible bidders must be willing and able to compete effectively for the business. However, contrary to these requirements, City officials published only two notices soliciting bids on January 7 and 28, 2013, in one local newspaper. Neither of the notices included details regarding the type of work required, and the second notice was published after the prebid meeting scheduled for January 15, 2013. As a result, the City received only one bid and awarded the contract to that bidder on March 21, 2013. City officials did not ensure that the procurement was conducted with full and open competition as required by Federal guidance.

While City officials had not initially intended to use Federal funds for this contract, they executed a change order on November 19, 2013, to include CDBG and Davis-Bacon Act requirements in the contract. However, they had made six payments on the contract, four of which totaling more than a million dollars were later reimbursed with CDBG funds. As a result, \$1.2 million in Federal funds was disbursed for a contract that was not procured in accordance with Federal procurement regulations and lacked required contract language. We attributed this deficiency to City officials' unfamiliarity with HUD regulations and lack of oversight when CDBG funding was later used to fund the contract. As a result, we could not determine whether the contract price was fair and reasonable or the sole-source method used by the City was justified. Therefore, the \$1.2 million disbursed for this contract is considered unsupported.

Further, City officials incorrectly entered the national objective for this loan into IDIS. The national objective was entered as SBS, slum or blight spot basis, instead of SBA, slum or blight area benefit. Regulations at 24 CFR 570.208(b)(2) do not include public facilities and improvements as eligible activities to address slum or blight on a spot basis. After learning of this error, City officials made the necessary correction in IDIS.

### **Inadequate Subrecipient Monitoring**

City officials did not perform adequate onsite monitoring of all of the City's CDBG subrecipients during our audit period and did not have adequate procedures in place to effectively track the status of subrecipient monitoring and any related findings. Regulations at 24 CFR 85.40 provide that grantees are responsible for managing the day-to-day operations of grant- and subgrant-supported activities and must monitor grant- and subgrant-supported activities to ensure compliance with applicable Federal requirements and ensure that performance goals are achieved for each program, function, or activity. While the City's 2013 and 2014 annual action plans provided that the City would monitor each subrecipient receiving Federal funds and conduct onsite visits to each subrecipient annually, the City's records provided that 19 of its 41 CDBG subrecipients had not received adequate monitoring during that period. For example, 13 of the 35 subrecipients under the City's Department of Neighborhood and Business Development were not included on the City's monitoring status tracking documents, and City officials informed us that the 6 subrecipients under the City's Department of Recreation and Youth Services had not received onsite monitoring during the previous few program years. In addition, the subrecipient monitoring documentation maintained by City officials did not adequately provide evidence of follow-up or resolution related to concerns and deficiencies identified.

### **Conclusion**

City officials had not established and implemented adequate controls to ensure that CDBG funds were always administered in accordance with applicable requirements. As a result, the City spent \$153,279 and more than \$8.1 million for ineligible and unsupported costs, respectively, and did not ensure that \$1.5 million was spent for its intended use. We attributed these deficiencies to weaknesses in accounting for disbursements, City officials' unfamiliarity with HUD regulations, and their failure to establish and implement adequate subrecipient monitoring procedures.

### **Recommendations**

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development instruct City officials to

- 1A. Reimburse from non-Federal funds \$153,279 spent on ineligible costs for duplicate and preaward costs of an economic development loan (\$99,616), non-Federal City salary costs (\$46,324), and duplicate subrecipient costs (\$7,339).
- 1B. Strengthen disbursement controls to ensure that CDBG funds are drawn down to reimburse only eligible costs.

- 1C. Provide documentation to justify the \$291,236 in unsupported costs related to disbursements made to the City's public services subrecipient. Any costs determined to be inadequately supported should be reimbursed from non-Federal funds.
- 1D. Strengthen procedures to ensure that all costs claimed for CDBG reimbursement are adequately supported by documentation before funds are disbursed.
- 1E. Provide documentation in the loan file that HUD approved the withdrawal of funds after the required deadline, and provide an explanation and obtain approval for the untimely disbursement of the \$6,724,820 after it had been drawn down. Any costs determined to be inadequately supported should be reimbursed from non-Federal funds.
- 1F. Strengthen controls to ensure compliance with Section 108 contract provisions and regulations requiring disbursement of funds in a timely manner after drawdown.
- 1G. Reimburse the \$1,500,000 in CDBG funds spent for the delinquent float loan that defaulted in 1998 through one of the options identified in HUD regulations so that it can be closed out as bad debt, thereby making the funds available for use on other eligible activities.
- 1H. Implement procedures to ensure that any future CDBG float-funded activities are administered in accordance with HUD regulations requiring that the annual action plan identify the float-funded activity and a commitment to undertake one of the options listed in the regulations if the funds are unable to be repaid within the required timeframe.
- 1I. Develop and implement procedures to ensure that the City's liens related to HUD-funded loans are not released without repayment or evidence of due diligence to address delinquent, outstanding loans.
- 1J. Provide documentation to support that the \$1,166,000 public facilities and improvements procurement contract price was fair and reasonable and that the sole-source method used was justified. Any costs determined not to be fair and reasonable should be reimbursed from non-Federal funds.
- 1K. Implement procedures to ensure that all HUD-funded procurement is performed in accordance with regulations at 24 CFR 85.36, which require that sealed bid procurements be adequately advertised and involve at least two bids and that independent estimates be documented before bids or proposals are received.
- 1L. Strengthen procedures over subrecipient monitoring to ensure that onsite visits are conducted for all CDBG subrecipients annually as specified in the agreements and that monitoring efforts are adequately tracked.

- 1M. Request CDBG program training from the HUD Office of Community Planning and Development field office relating to Section 108 and float loan administration, drawdown and disbursement of funds in a timely manner, and federal procurement regulations.

# Scope and Methodology

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We performed onsite audit work at the City's offices in Rochester City Hall located in Rochester, NY, between April and October 2015. The files and records related to the City's CDBG program are maintained at City Hall. The audit scope covered the period July 1, 2013, through March 31, 2015, and was extended as necessary. We relied in part on computer-processed data primarily for obtaining background information on the City's expenditure of CDBG funds. We performed a minimal level of testing and found the data to be adequate for our purposes. The results of sample testing were not projected to their respective populations. To accomplish our objective, we

- Reviewed relevant HUD regulations, guidebooks, and files.
- Interviewed HUD officials to obtain an understanding of and identify HUD's concerns with the City's operations.
- Reviewed HUD's central files for the City's CDBG program, including application, consolidated annual performance and evaluation report, audit, and monitoring files.
- Reviewed the City's policies, procedures, and practices.
- Interviewed key personnel responsible for administering the City's CDBG program.
- Reviewed expenditures in multiple program areas for compliance with regulations and program objectives, including public facilities and improvements, economic development, rehabilitation, and public services. We selected a sample by identifying the four CDBG program areas with the highest dollar amount of drawdowns during our audit period and then selected the activities with the highest dollar amount of drawdowns for each. This process resulted in a sample of 15 CDBG drawdowns on 4 different activities totaling more than \$4.6 million, or almost 25 percent of the more than \$18.5 million drawn during our audit period. We also reviewed the City's \$20 million Section 108 loan as more than \$3.4 million of it was drawn down during our audit period.
- Reviewed CDBG float-funded activities by selecting a sample consisting of the two most recent float loans and one float loan that had been identified as delinquent. The total CDBG funding related to these three loans was more than \$5.3 million. According to IDIS, the City had awarded 12 float loans since program year 1997 totaling more than \$11.4 million.
- Reviewed CDBG program income transactions for accuracy of recording and reporting. We selected a sample by identifying the monthly program income transactions totaling the largest dollar amount for each calendar year included in our audit period. This process resulted in a sample of 126 CDBG transactions totaling more than \$1.5 million, which

consisted of 8 receipts for \$815,814 and 118 drawdowns of \$747,713. During this period the City made 26 receipts totaling more than \$1.7 million and 444 drawdowns totaling more than \$2.2 million. We also reviewed the City's closeout of its revolving loan fund administered by a subrecipient based on the high risk level associated with both subrecipients and revolving loan funds.

- Reviewed the adequacy of the City's CDBG subrecipient monitoring program. We selected a sample of the City's CDBG subrecipient agreements by identifying the highest funded subrecipient during our audit period under each of the eight departments identified by the City on its subrecipient register. This process resulted in a sample of eight subrecipients awarded CDBG funds totaling more than \$1.2 million. The City's subrecipient register for our audit period included 46 subrecipient agreements totaling more than \$5.6 million in CDBG funds awarded.

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

# Internal Controls

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Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

## **Relevant Internal Controls**

We determined that the following internal controls were relevant to our audit objective:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding of resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

## **Significant Deficiencies**

Based on our review, we believe that the following items are significant deficiencies:

- The City did not have adequate controls over the effectiveness and efficiency of program operations when it did not establish adequate administrative controls to ensure that costs



associated with various program areas were supported and eligible under the CDBG program (finding).

- The City did not have adequate controls over the reliability of data when it inaccurately reported activity in IDIS (finding).
- The City did not have adequate controls over compliance with laws and regulations as it did not always comply with HUD regulations while disbursing CDBG funds (finding).
- The City did not have adequate controls to ensure that CDBG resources were safeguarded when funds were withdrawn after required deadlines, disbursements were made for ineligible and unsupported costs, and adequate collection efforts were not taken on delinquent loans (finding).

# Appendixes

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## Appendix A

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**Schedule of Questioned Costs and Funds To Be Put to Better Use**

<b>Recommendation number</b>	<b>Ineligible 1/</b>	<b>Unsupported 2/</b>	<b>Funds to be put to better use 3/</b>
1A	\$153,279		
1C		\$291,236	
1E		\$6,724,820	
1G			\$1,500,000
1J		\$1,166,000	
<b>Totals</b>	<b>\$153,279</b>	<b>\$8,182,056</b>	<b>\$1,500,000</b>

- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.
- 2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.
- 3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this case, if the recommendation to reimburse the \$1.5 million is implemented, City officials will be assured that the funds will be used for their intended purpose.

# Appendix B


## Auditee Comments and OIG's Evaluation

### Ref to OIG Evaluation

### Auditee Comments

Comment 1

Comment 2



**City of Rochester**  
City Hall Room 308A, 30 Church Street  
Rochester, New York 14614-1290  
www.cityofrochester.gov

Lovely A. Warren  
Mayor

January 20, 2016

Ms. Kimberly Greene  
Regional Inspector General for Audit  
U.S. Department of Housing and Urban Development  
Office of Inspector General  
Office of Audit  
New York/New Jersey Region 2  
26 Federal Plaza, Room 3430  
New York, NY 10278-0068

Dear Ms. Greene:

The City of Rochester is in receipt of the draft report from HUD as a result of the OIG audit during 2015. We have included our responses to the items listed in the draft report and will discuss in more detail at our January 25, 2016 exit conference.

Condition  
Funds Disbursed for Ineligible Costs-City officials disbursed \$153,279 in CDBG funds for ineligible costs.

Comment  
The City respectfully requests that the reimbursement from non-Federal funds of \$153,279 be reduced to \$0 as evidenced by the following information:

1. Reduce \$99,616.00 - for the costs identified in the Draft Audit Report for duplicate and pre-award costs of an economic development loan (Midtown Tower). Attached please find additional invoices and cancelled checks totaling \$288,193.68 for costs incurred after the City's amendment to the 2010-2011 annual action plan – these are the same costs originally transmitted to the auditor on October 9, 2015. This documentation covers the \$99,615.96 in the Ineligible costs category. When the factor of 43% is applied to the former amount for costs attributable to the commercial component of the development, this yields an adjusted amount of \$123,923.28 which is in excess of the \$99,616.
2. Reduce \$46,324 in salaries-Our Accounting office supplied the auditor with additional information on September 22, 2015 which indicated that during the third and fourth quarters of the covered period, the City drew \$897,986.79 for staff costs when in fact we had expenses of \$983,807.25. We claimed the lower amount as we reached our listed amount in the consolidated plan for those staff costs. The difference between what we drew and what we had expenses for more than makes up for the \$46,324 in salary costs listed above.
3. Reduce \$7,339 in costs paid to subrecipient---- Specifically in regards to contract #125446 in the amount of \$335,000 awarded to The Housing Council for Foreclosure Prevention Services we would like to dispute your findings with the following concerns:

Phone: 585.428.7045    Fax: 585.428.6059    TTY: 585.428.6054    EEO/ADA Employer    ♿

**Ref to OIG  
Evaluation**

**Auditee Comments**

Comment 3

Comment 4

Comment 5

Comment 6

Comment 7

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- a. "The subrecipient submitted 9 payment request for a total of \$335,000." Our records indicate 11 payment requests.
- b. "23 invoices totaling \$7,339 were duplicates." Upon another review of these invoices we did not find the duplicates indicated. We did however see incidents where the subrecipient provided 2 copies of invoices; one was a clean copy of the invoice and the second was a copy of the invoice with the cancelled check over it. It is possible this may have been a point of confusion.

"Documentation for other invoices was unorganized and did not clarify the amount claimed." This contract budgeted for \$45,839 in indirect cost. The indirect cost were paid in monthly increments of \$3,819.92. The City received and accepted a federally approved cost allocation plan allowing them to charge up to 18.46% of the total direct salaries and wage including fringe benefits as an indirect cost. This was provided upon review of the program documents. These costs do not require additional support documentation although it was presented. We believe this may have been the source of confusion. A copy of their indirect cost plan has been provided for further clarification. We would like the opportunity to either sit down with the auditor, or provide him with any further backup documentation to make a sound determination on this subject.

Condition

Funds Disbursed for Inadequately Supported Costs-City officials reimbursed a subrecipient administering the foreclosure prevention program \$291,236 in inadequately supported costs.

Comment

- 1. "While majority of cost claimed were for salaries, City's files did not include certification or timesheets for employees." Certified payroll registers were submitted and provided with each invoice for all personnel charged to this activity; however, personnel activity sheets which showed how time was allocated across funding sources were not. At the time of this contract the City did not require subrecipients to provide this information with each invoice. A monitoring visit was conducted at which time personnel activity reports were reviewed. The City has since changed its practice in this regard. All invoices are now accompanied by the certified time sheets. We would like the opportunity to either sit down with the auditor, or provide him with any further backup documentation to make a sound determination on this subject.
- 2. Disbursement controls have been strengthened as a result of continuous improvements in the disbursement process. In future loan agreements, CDBG funds will not be disbursed as construction financing without a comprehensive listing of all invoices and dates where there are multiple draws against one loan agreement. Disbursement controls on other CDBG funded contract have also been strengthened through continuous improvements to more adequately document expenses requested for reimbursement.
- 3. The City is continuing to strengthen the documentation for salary costs. Timesheets are being reviewed in an effort to eliminate errors, including mathematical errors, inconsistencies and missing signatures.

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**Auditee Comments**

Comment 8

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4. The matrix code used in IDIS for staff costs was rehabilitation administration. Past practice was to set up one activity in IDIS for program delivery. Only one matrix code can be chosen for each activity so a representative category was chosen. All program delivery was listed as rehabilitation administration. Beginning in the 2015-16 program year, the City of Rochester is setting up multiple activities in IDIS each with its own representative matrix code. This will more clearly show the actual expenses in each type of activity.

Condition

Section 108 Loan Funds Not Drawn Down and Disbursed in a Timely Manner nor Accurately Reported-City officials did not draw down and disburse Section 108 loan funds in a timely manner as required.

Comment

1. As stated in the draft report, City officials followed up with HUD and obtained written approval for an extension to the 108 loan. Documentation has been deposited in the loan file that HUD approved the withdrawal of funds after the required deadline regarding the disbursement of the \$6,724,820. We will provide the auditor with a CD that includes documentation on this grant.
2. The City will continue to strengthen controls to ensure compliance with Section 108 contract provisions and regulations requiring disbursement of funds in a timely manner after drawdown.

Condition

The City's CDBG Float Loans Inadequately Administered and Reported on-City officials did not adequately publicize action to document the City's procedures for collecting amounts due on CDBG float loans or take action to collect on delinquent loans in a timely manner.

Comment

1. It is currently the City's practice not to originate any new CDBG float loans. Should this practice change, the City will implement procedures to ensure that any future CDBG float-funded activities are administered in accordance with HUD regulations.
2. The City of Rochester will work with HUD Buffalo on options available to close out the \$1.5 million float loan.

Condition

Procurement Not Executed in Accordance with Federal Regulations-City officials disbursed \$1.2 million under a contract to develop an open space into an enhanced plaza that did not comply with Federal regulations.

Comment

1. Based on the audit finding related to the 1.2 million dollars in CDBG funds allocated to the open space area in the enhanced plaza as a part of the Midtown Redevelopment Project, DES has reviewed its internal processes and applying the policies and procedures against

Comment 10

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**Auditee Comments**

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those being formulated in the citywide Grants Manual by the Grants Management Team comprised of high level staff convened by the Director of Finance, Charles Benincasa. Training has been introduced and reinforced on an ongoing basis to all team members who are involved with CDBG Financials and will be ongoing.

The Midtown Phase 3 contract was bid in February, 2013. The City conducts competitive bidding under procedures pursuant to NYS General Municipal Law and Chapter 8A of the City of Rochester Municipal Code. These practices are consistent with 24 CFR 85.36(b). There was only 1 bidder. Work began in April, 2013. The original contract did not contain CDBG requirements. In November, 2013 the City added a no cost change order to the contract to incorporate CDBG requirements under 24 CFR Part 85.

Condition

Inadequate Subrecipient Monitoring-City officials did not perform adequate onsite monitoring of all of the City's CDBG subrecipients during our audit period and did not have adequate procedures in place to effectively track the status of subrecipient monitoring and any related findings.

Comment

1. The City is continually improving its management of monitoring to ensure monitoring of all subrecipients. In addition, we now have an Accounting monitoring component for monitoring of these entities.
2. DRYs staff have obtained a copy of the HUD guidebook for grantees on managing sub-recipients to better familiarize themselves with regulations. Since then, monitoring visits have been conducted with all current DRYs sub-recipients. Follow up letters summarizing the visits will be sent out within 30 days of the visit. This will continue to happen in future grant years.

Recommendations:

1A. Reimburse from non-Federal funds \$153,279 spent on ineligible costs for duplicate and preaward costs of an economic development loan (\$99,616), non-Federal City salary costs (\$46,324), and duplicate subrecipient costs (\$7,339).

In our response to the first condition listed above, we provide additional detail requesting that this recommendation be removed. We respectfully request that HUD review our additional documentation and remove this recommendation.

Comment 11

Comments 1,  
2 and 3



**Ref to OIG  
Evaluation**

**Auditee Comments**

Comment 12

Comments 6  
and 7

Comment 12

Comment 13

Comment 9

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1B. Strengthen disbursement controls to ensure that CDBG funds are drawn down to reimburse only eligible costs.  
Disbursement controls have been strengthened as a result of continuous improvements in the disbursement process. In future loan agreement, CDBG funds will not be disbursed as construction financing without a comprehensive listing of all invoices and dates where there are multiple draws against one loan agreement.

1C. Provide documentation to justify the \$291,236 in unsupported costs related to disbursements made to the City's public services subrecipient.  
We have provided comments in the conditions response to this letter. We would be happy to review with the auditor documentation for this program.

1D. Strengthen procedures to ensure that all costs claimed for CDBG reimbursement are adequately supported by documentation before funds are disbursed.  
The City acknowledges the comment above and will work to continuously improve our documentation of program expenses.

1E. Provide documentation in the loan file that HUD approved the withdrawal of funds after the required deadline, and provide an explanation and obtain approval for the untimely disbursement of the \$6,724,820 after it had been drawn down.  
Documentation has been deposited in the loan file that HUD approved the withdrawal of funds after the required deadline regarding the disbursement of the \$6,724,820.

1F. Strengthen controls to ensure compliance with Section 108 contract provisions and regulations requiring disbursement of funds in a timely manner after drawdown.  
The City will continue to strengthen controls to ensure compliance with Section 108 contract provisions and regulations requiring disbursement of funds in a timely manner after drawdown.

1G. Reimburse the \$1,500,000 in CDBG funds spent for the delinquent float loan through one of the options identified in HUD regulations so that it can be closed out as bad debt, thereby making the funds available for use on other eligible activities.  
The City will work with our HUD representatives to explore the options available to us to close out this issue.

1H. Implement procedures to ensure that any future CDBG float-funded activities are administered in accordance with HUD regulations requiring that the annual action plan identify the float-funded activity and a commitment to undertake one of the options listed in the regulations if the funds are unable to be repaid within the required timeframe.  
We acknowledge HUD's recommendation above. It is currently the City's practice not to originate any new CDBG float loans. Should this practice change, the City will implement procedures to ensure that any future CDBG float-funded activities are administered in accordance with HUD regulations.

1I. Develop and implement procedures to ensure that the City's liens related to HUD-funded loans are not released without repayment or evidence of due diligence to address delinquent, outstanding loans.  
The City acknowledges the above recommendation and should the City originate any new CDBG float loans, the City will implement procedures to ensure that any future CDBG float-funded activities are administered in accordance with HUD regulations.

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**Auditee Comments**

Comment 13

Comment 14  
Comment 13

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1J. Provide documentation to support that the \$1,166,000 public facilities and improvements procurement contract price was fair and reasonable and that the sole source method used was justified.

The City will submit additional information to HUD to document the steps taken by the City to ensure that this contract was awarded in a manner consistent with full and open competition and that the cost was reasonable.

1K. Implement procedures to ensure that all HUD-funded procurement is performed in accordance with regulations at 24 CFR 85.36, which require that sealed bid procurements be adequately advertised and involve at least two bids and that independent estimates be documented before bids or proposals are received.

The City provided a response to this recommendation earlier in this document. The City will provide documented support for the process subsequent to this communication.

1L. Strengthen procedures over subrecipient monitoring to ensure that onsite visits are conducted for all CDBG subrecipients annually as specified in the agreements and that monitoring efforts are adequately tracked.

The City of Rochester will work to strengthen above mentioned procedures and tracking efforts.

1M. Request CDBG program training from HUD Office of Community Planning and Development field office relating to Section 108 and float loan administration, drawdown and disbursement of funds in a timely manner, and federal procurement regulations.

The City of Rochester will work with our HUD field office to receive training issues mentioned above

The City of Rochester respectfully requests that OIG review the documentation provided in this letter and attached as previously sent emails to eliminate any ineligible costs findings. In addition, the City will work with HUD Buffalo on next steps to minimize control weaknesses in administering the CDBG Program.

Sincerely,



Brian F. Curran  
Acting Mayor

xc: Mayor Lovely A. Warren  
M. Fitzstevens  
J. Grzyb  
M.K. Kenrick  
B. Muhammad  
N. Jones  
K. Washington  
V. Wehbring



## OIG Evaluation of Auditee Comments

- Comment 1 City officials requested that \$99,616 identified in the report as duplicate and preaward costs be removed and provided documentation for additional eligible CDBG expenses to substitute for the questioned \$99,616. However, they did not provide additional documentation to support the eligibility of the \$99,616. Rather, they provided documentation for additional costs that were not provided during our fieldwork. Therefore, the \$99,616 remains as a questioned cost, and the eligibility of the additional costs will have to be determined by HUD during the audit resolution process.
- Comment 2 City officials requested that \$46,324 identified in the report as ineligible staff costs be removed because they had provided documentation to support additional eligible CDBG staff costs to substitute for those that had been deemed ineligible. However, because we received this documentation after we had completed our fieldwork at the City, these costs will remain in the report, and a final determination will be made as to their eligibility by HUD officials during the audit resolution process. Also, it should be noted that the staff costs identified as ineligible were drawn for the first and second quarters of the City's program year 2013, whereas the additional staff costs referenced by the City were incurred during the third and fourth quarters of the year.
- Comment 3 City officials stated that their records disclosed that the subrecipient submitted 11 payment requests, not 9. Review of documentation supported that 10 requests were made, and the report was changed to note that.
- Comment 4 City officials requested that \$7,339 identified in the report as duplicate costs paid to a subrecipient be removed, noting that there may be a misunderstanding because the subrecipient submitted two copies of invoices upon payment request. However, specific documentation to reconcile the payments was not provided.
- Comment 5 City officials stated that the determination that documentation was unorganized and unclear regarding the amount claimed may have been a misunderstanding caused by a federally approved cost allocation plan for indirect costs and they would like the opportunity to provide further clarification. However, this plan was not provided for review during our fieldwork. Therefore, the questioned costs will remain in the report, and the City will have an opportunity to provide additional documentation to HUD address any misunderstanding during the audit resolution process.
- Comment 6 City officials stated that certified payroll registers were provided for the CDBG subrecipient salary costs identified in our report but timesheets showing how time was allocated were not because the City's procedures did not require it. However, as mentioned in the report, certified timesheets are required by 2 CFR Part 225, appendix B, and City officials noted that the City has since changed its practice. In addition, while City officials stated that timesheets were reviewed as part of the

City's CDBG subrecipient monitoring for this activity, we were unable to locate documentation showing that this review occurred. Therefore, a final determination regarding the eligibility of the questioned costs and adequacy of the related procedural changes will be made by HUD during the audit resolution process.

- Comment 7 City officials stated that they have strengthened controls over disbursements to subrecipients, are continuing to strengthen documentation for salary costs, and will set up multiple activities in IDIS to more clearly show the actual expenses in each type of activity. The adequacy of these actions will need to be verified by HUD during the audit resolution process.
- Comment 8 City officials agreed with our report since they had followed up with HUD and obtained written approval for an extension to the City's Section 108 loan after the deadline had passed and they had drawn down the funds. They stated that documentation supporting this approval was placed in the loan file and they would strengthen their controls over the administration of the City's Section 108 loans. We acknowledge that City officials have been proactive and responsive to all of our recommendations. However, a final determination will be made by HUD officials during the audit resolution process regarding the adequacy of the documentation and procedural changes to strengthen controls.
- Comment 9 City officials stated that it is not the City's practice to originate new CDBG float loans but they would implement procedures to ensure that these loans are administered in accordance with HUD regulations if this practice changes. City officials also stated that they would work with HUD officials on options to close out the delinquent \$1.5 million float loan identified. This action is responsive to our recommendation.
- Comment 10 City officials stated that the City's Department of Environmental Services has reviewed its internal processes and introduced training based on our review of the \$1.2 million public facilities and improvements procurement contract identified in the report. They also stated that the City conducts competitive bidding under State and local procedures in accordance with 24 CFR 85.36(b). However, this regulation states that grantees will use their own procurement procedures, which reflect applicable State and local laws and regulations, provided that the procurements conform to applicable Federal law. Therefore, the bidding and advertising deficiencies identified in this report were still applicable to the City.
- Comment 11 City officials stated that they are continuously improving the City's management of subrecipient monitoring and they have made related procedural changes. Determination of the adequacy of these procedures will be made by HUD officials during the audit resolution process.
- Comment 12 City officials stated that disbursement controls have been strengthened. This is responsive to our recommendation, and determination of the adequacy of these improvements will be made by HUD officials during the audit resolution process.

- Comment 13 The proposed action is responsive to our recommendation. The adequacy of this action will be determined by HUD officials during the audit resolution process.
- Comment 14 City officials requested that HUD OIG review the additional documentation provided with the City's written comments to eliminate any ineligible cost findings in the report. However, this material was not made available during our fieldwork. Therefore, final determination as to its responsiveness to the recommendations will have to be made by HUD during the audit resolution process.