

**U. S. Department of Housing and Urban Development
Office of Inspector General**



**Monitoring of Local Governments under the State CDBG
Program**

**Kenneth M. Donohue, Sr.
Inspector General**

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Executive Summary

The Office of Inspector General, Inspections and Evaluations Division, conducts independent, objective examinations of U.S. Department of Housing and Urban Development (HUD) activities, programs, operations, or organizational issues.

We completed a nationwide inspection of the monitoring conducted by State agencies of units of general local government (referred to in this document as local grant recipients) under the State Community Development Block Grant (CDBG) program. Monitoring is one method used by States to ensure compliance with program regulations and assists agencies in the detection and prevention of fraud.

The objective of this inspection was to determine the types and extent of monitoring utilized by the States to ensure the proper use of CDBG funds by local grant recipients. The inspection also set out to determine whether the monitoring efforts resulted in any remedial actions taken by the States. The review focused on the monitoring efforts carried out by the States during their 2004 and 2005 program years and did not evaluate the effectiveness of their monitoring.

We determined that, except for the need to improve their monitoring of the receipt of single audit reports from local grant recipients, the participating States are essentially adhering to the basic Federal monitoring requirements. Almost all of the participating States have conducted on-site monitoring visits during their 2004 and 2005 program years, and all 49 participating States and Puerto Rico submitted their annual performance and evaluation reports to HUD. While the States have assigned staff to monitor the local grant recipients, a total of six States advised that inadequate resources have hindered their ability to monitor the local grant recipients. It was also noted that five of the nine States we contacted issued sanctions against local grant recipients for not complying with program requirements or achieving program objectives.

If you have any questions concerning this report, please call Special Agent in Charge, Kenneth Taylor Jr., at (202) 402-8416.

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Introduction

The Community Development Block Grant program (CDBG), created in 1974, provides funds for housing rehabilitation, neighborhood revitalization, economic development activities, and improved community facilities and services. Statutory requirements for CDBG appropriations include funds reserved for Indian tribes, insular areas, and set-asides. The balance of the appropriated funds is then allocated 70 percent to metropolitan cities and urban counties for the Entitlement program and 30 percent to States for use in non-entitlement areas. The State CDBG program, which is the subject of this review, allows each State the option to directly administer the block grant funds for its non-entitlement areas. These non-entitlement areas generally include counties with populations under 200,000 and cities with populations under 50,000.

Forty-nine States and Puerto Rico have elected to administer the State CDBG program. Hawaii has made a permanent election not to administer the program. Hawaii's share of the non-entitlement allocation is awarded directly to the three Hawaiian counties, which are otherwise treated as entitlement communities.

For fiscal years 2004 and 2005, Congress appropriated more than \$4 billion annually for the entire CDBG program. The State CDBG program was allocated about \$1.29 billion from the fiscal year 2004 appropriations and about \$1.23 billion from the fiscal year 2005 appropriations. The individual State block grants are allocated based on a statutory formula. The States design and implement their own programs for distributing the CDBG funds to their eligible counties and cities (referred to as units of general local government). States are required to pay all administrative costs incurred by the State in carrying out its responsibilities from its own resources. However, the States may use up to \$100,000 of their CDBG grant funds for administrative purposes. In addition to this amount, up to 3 percent of the grant may be expended at the State level for administrative costs, provided that the State matches these funds with its own resources.

Whereas HUD's role is essentially limited to ensuring that the States comply with Federal laws, regulations, and policies, the States administering the program are responsible to ensure that local grant recipients comply with applicable State and Federal laws and requirements.

The monitoring of a program can encompass a number of different practices and methods. The Federal regulations describing the States' responsibilities in monitoring the use of CDBG funds by local grant recipients are found in 24 CFR (*Code of Federal Regulations*) Part 570, Subpart I – State CDBG Program.

- 24 CFR 570.492 prescribes the States' responsibilities to conduct reviews and audits of local grant recipients. These responsibilities include on-site reviews of local grant recipients and the submission to HUD of annual performance and evaluation reports.

- 24 CFR 570.489(m) prescribes that audits of the States and local grant recipients shall be conducted in accordance with 24 CFR 85.26, which implements the Single Audit Act, as required by Office of Management and Budget (OMB) Circular A-133, “Audits of States, Local Governments and Non-Profit Organizations.”
- 24 CFR 570.492 provides the States with the authority and responsibility to take actions to remedy instances of noncompliance by local grant recipients.

These regulations are supplemented by HUD’s guidance, which advocates close monitoring of the local grant recipients by the responsible States.

Scope and Methodology

To achieve our objectives, we first identified the basic Federal statutory and regulatory requirements for the monitoring of the local grant recipients by the participating States. We then compared data collected for all of the participating States and Puerto Rico to the Federal requirements.

We designed a questionnaire to gather the majority of the information we analyzed and used in this inspection. The questionnaire was sent to the 35 Office of Community Planning and Development (CPD) regional/field offices that have program responsibility over the State CDBG program to collect information on the monitoring efforts of the 49 States and Puerto Rico.

We supplemented the data collected from the CPD offices by sending a similar questionnaire to nine judgmentally selected States (Appendix A). The questionnaire used to collect data from the nine States also contained a number of questions on State staffing resources and training as well as information on sanctions taken by States against local grant recipients that the HUD CPD offices did not have available. We selected these States by giving consideration to the amount of State CDBG funds allocated to the States and the number of grant recipients in each State and by giving coverage to nine of the ten HUD geographic regions.

The table on the next page shows the nine States that we selected and the responsible HUD regional office. The funding allocated to the nine States represented more than 20 percent of the total State CDBG program funds allocated by HUD in program years 2004 and 2005.

HUD region	State	2004 program year funds (millions)	2005 program year funds (millions)
1	Maine	\$16.9	\$15.7
2	New Jersey	\$9.4	\$9.0
3	West Virginia	\$19.9	\$19.0
4	Tennessee	\$31.3	\$29.8
5	Ohio	\$57.1	\$54.6
6	Texas	\$86.7	\$82.3
7	Kansas	\$20.2	\$19.2
8	Wyoming	\$3.8	\$3.6
9	California	\$49.9	\$46.8
	Total	<u>\$295.2</u>	<u>\$280.0</u>

We achieved a 100 percent response rate from the 35 CPD offices and the nine States.

We sorted and then analyzed HUD's CDBG Activity Summary Report (PR03) for 40 of the 49 participating States and Puerto Rico, representing about 84 percent of the total CDBG funds allocated to all participating States in program years 2004 and 2005. This analysis was conducted to obtain a count of the number of local grant recipients that expended funds in those States. The Activity Summary Reports disclosed that on average, each State was responsible for monitoring more than 200 local grant recipients. We also used this report to supplement the information provided to us by the States relating to local grantee compliance with the reporting requirements of the Single Audit Act (i.e., local grant recipients that expended more than \$500,000 in Federal funds during a year).

We reviewed past reports issued by both HUD's Office of Inspector General (OIG) and the U.S. Government Accountability Office (GAO) since 1997 that assessed the monitoring of the overall CDBG program. This review was conducted to determine whether there were any systemic problems associated with the monitoring of local grant recipients under the State CDBG program. These reports focused primarily on the monitoring efforts of HUD and the local grant recipients rather than the monitoring conducted by the States. Accordingly, these reports did not identify systemic problems specific to State monitoring of local grant recipients.

We also contacted several professional associations that represent State and local grant recipients to determine whether studies had been conducted that collected data on monitoring by the States. These professional associations had not collected data on monitoring or assessed the States' monitoring of the local grant recipients.

We consulted with staff from HUD's headquarters CPD State and Small Cities Division to obtain program and policy information as it related to the monitoring of the program

and to obtain funding data for the States and local grant recipients. The CPD staff reviewed the questionnaires and assisted in coordinating the transmission of the questionnaires to the HUD CPD regional/field offices. We also consulted with the CPD Office of Deputy Assistant Secretary for Operations regarding the OMB Federal Audit Clearinghouse (FAC). Staff from the CPD office assisted us in accessing the FAC computerized database to determine whether the local grant recipients had submitted the required annual single audit reports.

We conducted this inspection in accordance with the Quality Standards for Inspections issued by the President's Council on Integrity and Efficiency. The nationwide inspection was performed generally between October 2006 and July 2007.

Observations

Observation 1: Types of State Monitoring Efforts

A. On-Site Monitoring Reviews

Federal regulations provide for the individual State to make decisions on the necessity of making on-site monitoring visits to particular local grant recipients. 24 CFR 570.492 requires States to perform on-site reviews of local grant recipients only as the State believes it to be necessary or appropriate to ensure the proper and timely use of the program funds. However, HUD guidance found in HUD Handbook 6509.2, REV-5, chapter 4, states that while HUD does not require States to conduct on-site visits to all local grant recipients every year, HUD does expect the States to make at least one on-site visit to all local grant recipients before the closeout of the funded project.

The HUD CPD offices reported that during program year 2004, at least 36 States conducted on-site monitoring visits to local grant recipients in their States. During program year 2005, a total of 33 States made similar visits. The CPD offices did not have information on the remaining participating States.

In addition to the State-initiated on-site visits, the CPD offices reported that during program years 2004 and 2005, more than 10 States each year accompanied CPD field office staff on monitoring site visits to local grant recipients.

All nine States surveyed conducted on-site monitoring visits to local grant recipients. Overall, during both program years, the nine States conducted on-site monitoring visits to approximately 46 percent of their active local grantees. A large majority (more than 96 percent) of the on-site monitoring visits performed during program years 2004 and 2005 by State staff were made prior to the closeout of a specific CDBG-funded project. In addition, two of the States reported that their staff also accompanied HUD CPD staff on monitoring visits to local grant recipients. We also noted that five of the nine States conducted risk analyses of the local grant recipients to determine which grantees would receive closer oversight.

B. Annual Performance and Evaluation Reports

Federal regulations at 24 CFR Part 91 mandate that each participating State submit to HUD a consolidated plan, which includes a description of the standards and procedures States will use to monitor the activities of the local grant recipients. As part of the requirement, each State that prepares a consolidated plan shall annually review and report to HUD on the progress it has made to carry out its plan. Federal regulations at 24 CFR 570.491 also require that the States submit to HUD annual performance and evaluation reports. The performance and evaluation report should include a description of how the program funds were used and the progress made to accomplish the program's objectives during the past program year.

The 35 HUD CPD offices reported that for both program years 2004 and 2005, all 49 participating States and Puerto Rico submitted their performance and evaluation reports.

C. Annual Single Audit Reports

OMB Circular A-133, "Audits of States, Local Governments and Non-Profit Organizations," revised June 27, 2003, requires Federal award recipients to have independent audits performed if they expend \$500,000 or more in Federal funds during a year. Furthermore, Circular A-133 holds the States, as designated "pass-through" States, responsible for monitoring the activities of the local grant recipients and ensuring that the single audits are conducted. The audited local grant recipients are responsible for submitting the completed single audit reports to the OMB FAC and to their "pass-through" State within 9 months after the end of the audit period.

All nine States had local grant recipients that expended more than \$500,000 in one or both of the years we included in our review. For four of the nine States surveyed, we found that for the years 2004 and/or 2005, some local grant recipients did not submit the required single audit reports to the FAC. For example, West Virginia had a submission rate of 70 percent for 2005, and Wyoming's rate was 80 percent for 2004. West Virginia reported that the State auditor's office had not yet issued contracts to have the audits conducted of the delinquent local grant recipients. Ohio indicated that it was pursuing the delinquent audit report submissions with the local grantees.

Three States had a single audit report submission rate of 100 percent for both 2004 and 2005. Two States (Tennessee and California) did not have information on whether the required single audit reports had been submitted. These States rely on their State controller's office to administer the Federal single audit requirement.

The following table shows the results of our State survey questions on the single audit requirement:

State	Year	Number of local grantees required to submit single audit reports	Number of local grantees that submitted single audit reports	Number of local grantees that did not submit required single audit reports	Percentage of local grantees that submitted the required single audit reports
Texas	2004	194	189	5	97%
	2005	172	168	4	98%
Kansas	2004	31	31	0	100%
	2005	26	26	0	100%
New Jersey	2004	10	10	0	100%
	2005	6	6	0	100%
Maine	2004	39	39	0	100%
	2005	39	39	0	100%
West Virginia	2004	14	14	0	100%
	2005	10	7	3	70%
Tennessee	2004	Information not available	Information not available	Information not available	Information not available
	2005	Information not available	Information not available	Information not available	Information not available
California	2004	Information not available	Information not available	Information not available	Information not available
	2005	Information not available	Information not available	Information not available	Information not available
Wyoming	2004	15	12	3	80%
	2005	0	0	0	Not applicable
Ohio	2004	117	116	1	99%
	2005	137	123	14	90%

Note: Single audit reports are required to be submitted no later than 9 months after the completion of the audit period.

To supplement the results of the State survey, we conducted an analysis of HUD's CDBG Activity Summary Report and the OMB FAC database. While HUD's data indicated a lower rate of audit reports being submitted in some States in comparison to the above data, the differences may be due to two factors: the 12-month audit period for the local grant recipients in some instances are different from the program year timeframe used in

HUD's CDBG database, and according to CPD officials, there may be delays in the downloading of the audit reports after receipt by the FAC.

D. Other Monitoring Methods Employed by States

One of the intentions of the State CDBG program is to allow the States, and not HUD, to manage and operate the program in their individual States. While there are basic Federal requirements for State monitoring, the States are permitted some discretion as to the extent and methods of monitoring that they are to employ. Federal regulations at 24 CFR 570.492 cite that States shall make reviews and audits as may be necessary or appropriate to meet the requirements of the program.

All nine States reported that in addition to on-site monitoring visits and reviews of the single audit reports, they conducted desk reviews of financial and program data provided by the local grant recipients. Some of these States also used training workshops and technical assistance visits to the local grant recipients as a means to monitor the grantees.

Observation 2: Extent of State Resources Devoted to Monitoring

The nine States surveyed all reported that they assigned staff to monitor the local grant recipients in their States. However, three of the nine States (i.e., Texas, California, and Wyoming) reported that the lack of adequate resources hindered their ability to monitor the local grant recipients. The lack of resources dealt primarily with insufficient funds to conduct more on-site monitoring visits. Additionally, the CPD offices in response to our questionnaire identified three other States in which the lack of resources hindered their monitoring of local grant recipients (i.e., Nevada, Alaska, and Michigan).

While the data obtained from the nine States also showed that each staff member on average was responsible for monitoring approximately 18 local grantees, the range varied greatly from a low of six in New Jersey to a high of 58 in Kansas. All nine States provided training for the staff in monitoring. The number of training hours received by individual staff ranged from 1 hour per year to a high of 62 hours, and for three States, HUD provided additional training.

Observation 3: State Remedial Actions and Sanctions

24 CFR 570.492 specifies that State agencies have the authority to take actions to remedy instances of noncompliance by grant recipients and to prevent future occurrences of noncompliance.

Five of the nine States surveyed took remedial action against local grant recipients for noncompliance issues. Findings of noncompliance included failure to achieve the primary program objectives and conflict of interest between the local grant recipient and contractors. The sanctions taken to remedy the situations included repayment of funds not used properly and the suspension of future funding.

It was also noted that HUD had taken remedial actions against four States because certain local grantees were not in compliance with HUD CDBG regulations and requirements. These actions included voluntary grant reductions for inadequate internal controls and not complying with environmental requirements. One State was required to pay back funds because a local grant recipient misused the program funds for inappropriate purposes.

Recommendations

We recommended that the Director, Office of Block Grant Assistance, require the CPD regional/field offices to

1. Ensure that all of the State administering agencies establish a system to monitor the receipt of annual single audit reports submitted by the local grant recipients. In this regard, the States cited in this report with delinquent audit reports (refer to the table in observation 1c) should be required to follow up with all of their local grantees to ensure compliance with OMB Circular A-133 single audit requirements.
2. Determine the needs of the six States which indicated that limited resources have hindered their monitoring efforts (refer to observation 2) and assist these States in developing a plan and method to effectively utilize the resources available.

As a result of our recommendations, the Office of Block Grant Assistance responded that

1. CPD will issue guidance to emphasize the requirements of OMB Circular A-133. States are required to have a system to monitor the receipt of the annual single audit reports. CPD monitors this during its review of States' financial management systems. CPD's monitoring Handbook 6509.2, REV-5, exhibit 4-7, covers the States' financial systems.
2. CPD will work with the applicable field offices to determine how the identified States can maximize their use of administrative funds for both on-site and desk monitoring reviews.

Appendix A

Nationwide Inspection of State Monitoring Under the State CDBG Program

State Administering Agency Questionnaire

The Inspections and Evaluations Division of the HUD Office of Inspector General (OIG) is conducting a nationwide inspection of the monitoring of units of general local government (referred to as grant recipients) conducted by state agencies that administer the State Community Development Block Grant (CDBG) Program

The OIG's authority to have access to all program data is prescribed in 24 CFR 570.490 (c) which in part states that representatives of the OIG shall have access to all records, reports, files, and other papers pertaining to the administration, receipt and use of CDBG funds

As you are aware, in accordance with 24 CFR 570.480, states can elect to administer CDBG funds in non-entitlement areas of their states. Sections 491 and 492 of 24 CFR 570 prescribe the states' responsibilities to make reviews and audits of grant recipients. This includes on-site reviews of grant recipients, submission to HUD of annual performance and evaluation reports, and annual single audits conducted by states and grant recipients if the funds expended exceed the annual threshold.

24 CFR 570.492 also specifies that state agencies have the right to take such actions, as determined by the state, to remedy instances of non-compliance by grant recipients.

As part of this inspection, questionnaires have been sent to a select number of state agencies that have program responsibility over the State CDBG Program. The primary purpose of the questionnaire is to collect information on the monitoring efforts of states of the grant recipients, covering a two-year period for states' Program Year's 2004 and 2005. The selection of the states was based on collecting information from a cross section of states by the amount of State CDBG funds allocated to the states, number of grant recipients in the state and the location of the states.

Questionnaire Instructions

The questionnaire is designed to be responded to electronically and is formatted in Microsoft Word.

1. Answer all questions on your computer.
2. All answers should be recorded within the tables and grids placed under each question.
3. Answer all the questions. If you do not have or know the answer to a particular question, please indicate in the space provided.
4. For questions that require narrative answers, please keep the answers as brief as possible while completely answering the question.
5. Please complete the questionnaire by March 7, 2007 and transmit the completed questionnaire to the email address shown below.
6. Provide a point of contact in your office if follow-up questions and/or information are required.

NKrieger@hudoig.gov

Mailing address is:

U.S. Department of Housing and Urban Development
Office of Inspector General, Suite 3437
Attn: Norman Krieger
26 Federal Plaza
New York, New York 10278

Please provide responses to the following set of questions for your state and where applicable, the grant recipients in your state for your Program Year's (PY) 2004 and 2005.

1. Identify the name of the state agency responsible for administering the State CDBG Program in your state.

State	State administering agency	Point of Contact

2. Identify the grant recipients, in your state that received State CDBG Program funds and the amounts awarded and expended during Program Years' 2004 and 2005.

Grant recipient	PY2004 grant amounts awarded	PY2004- grant amounts expended	PY2005 – grant amounts awarded	PY2005 – grant amounts expended

Please add as many rows as necessary to report on all the grant recipients in your state for Program Years' 2004 and 2005. If it is more convenient, you can provide the funding data in a computerized data base as a supplement to this questionnaire.

3. For both Program Years' 2004 and 2005, show the number of staff who participated in the monitoring of grant recipients.

Program Year	Number of staff who monitored grant recipients
2004	
2005	

4. For both Program Years' 2004 and 2005, show amount of funds expended for monitoring the grant recipients.

Program Year	Amount of funds expended for monitoring grant recipients
2004	
2005	

5. For both Program Years' 2004 and 2005, show the number of hours of training provided to your staff on how to monitor grant recipients. This should include both in-house and external training (if provided by HUD, specify).

Program Year	Total hours of training provided to staff on monitoring	Indicate total hours of training that was provided by HUD
2004		
2005		

6. Did your state conduct a risk analysis to help determine the level of monitoring for individual grant recipients?

Program Year	Risk analysis conducted Yes or No
2004	
2005	

7. Did your state submit an annual single audit report that included the State CDBG Program for either Program Years' 2004 and 2005?

Program Year	Yes or No
2004	
2005	

- a. If your state did not submit the single audit report for either Program Years' 2004 or 2005, indicate why the state did not submit the audit report.

PY2004 – Explanation	PY2005 – Explanation

8. Show the grant recipients in your state that submitted the annual single audit reports, if their Program Year expenditures exceeded \$500,000 in federal funds, including the State CDBG Program funds.

PY2004 – Grant recipients that submitted single audit reports	PY2005 – Grant recipients that submitted single audit reports

Please add as many rows as necessary to report on all the grant recipients in your state for Program Years 2004 and 2005.

- a. Identify any grant recipients that did not submit a required single audit in either Program Years' 2004 or 2005, if they exceeded the \$500,000 threshold on federal expenditures in a single Program Year.

PY2004 – Grant recipients that did not submit the required single audit report	PY2005 – Grant recipients that did not submit the required single audit report

Please add as many rows as necessary to report on all the grant recipients in your state for Program Years 2004 and 2005.

9. Although states are not required to conduct on-site visits to each grant recipient each year, HUD does expect states to conduct an on-site visit before project closeout.
- a. Show the number of on-site monitoring visits that were made by your state during Program Years 2004 and 2005, to grant recipients. Identify if such visits were made prior to the closeout of the funded project.

State	PY 2004 all on-site visits	PY 2004 on-site visits prior to project closeout	PY 2005 all on-site visits	PY 2005 on-site visits prior to project closeout

10. Did your state participate with HUD in on-site monitoring visits to specific grant recipients prior to project closeout during Program Years' 2004 and 2005?

PY2004 – Number of on-site visits with HUD to grant recipients	PY2005 – Number of on-site visits with HUD to grant recipients

11. Did your state submit the required annual performance and evaluation reports (PER) to the HUD regional or field offices for either Program Years' 2004 and 2005.

PY2004 – Submit the PER -Yes or No	PY2005 – Submit the PER - Yes or No

- a. If your state did not submit an annual PER for either Program Years' 2004 or 2005, indicate the reason why the state did not submit the report.

PY2004 – Reason(s) why PER not submitted	PY2005 – Reason(s) why PER not submitted

12. Identify remedial actions (per 24.CFR.570.492) that your state took during Program Years' 2004 and 2005 against grant recipients for non-compliance of the CDBG program requirements.

Grant recipients	Actions in PY2004	Actions in PY2005

Please add as many rows as necessary to report on all the grant recipients in your state for Program Years' 2004 and 2005.

13. Identify any other methods, beyond those mandated by federal statute and regulation that you employed to monitor the grant recipients in your state during Program Years ending in 2004 and 2005.

PY 2004	Description of other methods of monitoring used
PY 2005	Description of other methods of monitoring used

14. Provide any further comments or observations about monitoring of grant recipients in your state, including identifying any barriers to effective monitoring.

Acknowledgements

This inspection was conducted under the direction of Ruth A. Ritzema, Deputy Assistant Inspector General for Inspections and Evaluations, Office of Investigation.

Michael Groszkiewicz, Special Agent in Charge, Inspections and Evaluations Division, Office of Investigation, supervised the assignment.

The following OIG field office staff conducted the inspection and prepared the report:

Mark Klein, Supervisory Forensic Auditor
Norman A. Krieger, Senior Forensic Auditor
Ann Marie Hamilton, Forensic Auditor
Lisa Tong, Forensic Auditor