



Issue Date	February 9, 2011
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Audit Report Number	2011-KC-1001
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TO: Ray E. Willis, Director, Region V, Office of Community Planning and Development, 5AD

FROM: //signed//
Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

SUBJECT: The City of East St. Louis, IL Did Not Properly Manage Housing Rehabilitation Contracts Funded by the Community Development Block Grant Program

HIGHLIGHTS

What We Audited and Why

We audited the City of East St. Louis' (City) Community Development Block Grant (Block Grant) program because it is the 10th largest recipient in the State of Illinois and is the largest Illinois recipient of Block Grant funds outside the Chicago area.

The objective of our review was to determine whether the City properly managed Block Grant-funded housing rehabilitation contracts.

What We Found

The City awarded more than \$1 million in Block Grant funds for 124 of the 147 rehabilitation contracts reviewed without adequately ensuring that it complied with requirements and that the work was completed in an acceptable manner. Specifically, it did not ensure that contractors completed all of the contracted work as required and at a reasonable cost. Additionally, the City created scopes of work for the rehabilitation contracts that were not detailed and specific in

nature. Finally, it did not comply with Federal procurement requirements and its own policies and procedures when it managed the rehabilitation contracts.

What We Recommend

We recommend that the U.S. Department of Housing and Urban Development (HUD) withhold \$400,000 in 2010 Block Grant funding for the City's housing rehabilitation programs until it improves its controls and require the City to collect more than \$127,000 paid to contractors for rehabilitation work not performed or improperly performed. Additionally, we recommend that HUD require the City to develop and implement adequate internal controls to ensure that all work is completed according to the scope of work, update its inspection software, and provide training to ensure future compliance.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided the draft audit report to the City on January 14, 2011 and requested its comments by January 28, 2011. The City provided its written comments on January 28, 2011. It generally disagreed with our findings.

The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVE

Title I of the Housing and Community Development Act of 1974 established the Community Development Block Grant (Block Grant) program, a flexible program that provides communities with resources to address a wide range of unique community development needs. According to 24 CFR (Code of Federal Regulations) 570.202(a)(1), one permitted use of Block Grant funds is to finance the rehabilitation of privately owned buildings and improvements for residential purposes.

The City of East St. Louis (City) participates in the Block Grant program as an entitlement community. These grants are allocated to larger cities and urban counties to develop viable communities by providing decent housing, a suitable living environment, and opportunities to expand economic opportunities, principally for low- and moderate-income persons. The U.S. Department of Housing and Urban Development (HUD) determines the amount of each entitlement grant by a statutory dual formula which measures community needs in relationship to those of other metropolitan areas. The City received almost \$3.7 million for fiscal years 2007 and 2008 combined. It used these funds for several purposes including housing rehabilitation, code enforcement, and public services.

The City's Block Grant program is administered by its Community Development Department. Additionally, the City is subject to the Financially Distressed City Law and is accordingly under the control of the State-established East St. Louis Financial Advisory Authority, which provides oversight and assistance. The City had a home repair program, senior modification program, and emergency home repair program with maximum grant amounts of \$15,000, \$9,999, and \$9,999, respectively, in 2008. Through these housing rehabilitation programs, the City addressed the national objective of addressing substandard housing concerns and ensuring decent housing and a suitable living environment for low- to moderate-income homeowners. The City does not conduct the rehabilitation activities with its own labor but solicits bids from contractors to participate in the home rehabilitation programs.

This is our third audit report on the City's Block Grant program. Our first report disclosed that the City did not properly allocate \$917,669 and \$58,205 in salary and building expenses, respectively, or properly document its process for securing a \$49,924 consulting services contract (report number 2010-KC-1003, dated March 26, 2010). Our second report disclosed that the City improperly awarded more than \$1.2 million in Block Grant program funds to recipients of rehabilitation work without adequately verifying their eligibility (report number 2010-KC-1008, dated September 28, 2010).

Our objective was to determine whether the City properly managed Block Grant-funded housing rehabilitation contracts.

RESULTS OF AUDIT

Finding 1: The City Improperly Expended Block Grant Program Funding for Housing Rehabilitation Projects

The City expended Block Grant funds for 116 housing rehabilitation projects that were not completed, were improperly completed, or were completed at an unreasonable cost. This condition occurred because the City had inadequate controls over the contracting process. As a result, homeowners did not get the repairs they were entitled to, their lives could be at risk from substandard work, and HUD had no assurance that more than \$1 million in Block Grant funds was well spent.

Of 132 projects we physically inspected, the City expended Block Grant funds for 116 housing rehabilitation projects that were not completed, were improperly completed, or were completed at an unreasonable cost. It granted these contracts in East Louis, IL, via sealed bids. The assisted homes were selected for improvement through the home repair, senior modification, and emergency home repair programs. Appendix C contains a schedule of the deficiencies identified in each of the 116 projects.

Incomplete Rehabilitation Work

The City paid contractors for rehabilitation work that was not completed in 30 assisted houses. The contractors did not complete invoiced work items including guttering, electrical, plumbing, and window work. For example, for project #1843, part of the contract required the contractor to install new vinyl siding over the entire structure. The contractor did not install the vinyl siding. For project #1692, part of the contract required the contractor to rewire the entire house. The contractor did not rewire the house, and the homeowner had to hire an electrician to do the rewiring. In both cases, the City paid the contractor the full contract amounts of \$9,909 and \$6,500 respectively.



Vinyl siding was not installed around the entire house in project #1843.

Substandard Rehabilitation Work

The City paid contractors for rehabilitation work that was not completed in a workmanlike manner in 99 projects. The poorly completed work included substandard electrical, roof, and plumbing work. For example, for project #1714, part of the contract required the contractor to replace the toilet with a handicapped toilet and a grab bar. The replacement toilet did not comply with handicapped height requirements, and there was no grab bar. For project #1832, the contract required the contractor to replace the front and rear covered porches. On the front porch, the contractor improperly installed the columns. In addition, some porch ceiling boards were deteriorated and needed to be replaced. Instead, the contractor cut strips of oriented strand board and screwed them to the surface of the ceiling. The contractor used plywood sheets to build both porches' floors instead of using parallel boards with small gaps between them for drainage. The column blocks on the right side of the rear porch sat on the soil and were starting to settle, causing it to start leaning.



A nonhandicapped toilet and no grab bar were installed in project #1714.



Strips of oriented strand board were screwed to the front porch ceiling of project #1832.



For project #1832, the contractor straddled boards from one side of the pier formwork to the other and rested the columns on the boards instead of on the front porch's concrete piers.

Overpriced Rehabilitation Work

The City expended Block Grant funds for repairs that were completed at an unreasonable cost on 84 projects. In these homes, the City paid the contractor more than our estimated cost of completion for the completed work items. The 30 projects with incomplete rehabilitation work and the 99 projects with substandard rehabilitation work are not mutually exclusive and add up to a total of 104 projects. Of the 104 projects with incomplete and substandard rehabilitation work, the City paid the contractors more than the value of the work completed on 72 of the projects. On 12 additional projects, the contractors provided the contracted work but at an unreasonable price. For example, for project #1605, the contractor was required to tear off the existing roofing, replace

deteriorated roof sheathing, and install new shingle roofing at a cost of \$7,630. We estimated that the contract should have cost no more than \$5,883; therefore, the City overpaid \$1,747.

Regulations at 2 CFR 225, Appendix A, (c)(2), state that a cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. It also adds that when determining reasonableness, consideration must be given to the market prices of comparable goods and services as well as if the individuals concerned acted with prudence in the circumstances considering their responsibilities to the governmental unit, its employees, the public at large, and the Federal Government.

Inadequate Controls Over the Contracting Process

The City had inadequate controls over the contracting process.

Inadequate Supervision

The City did not adequately supervise its inspector. It had no quality control policies and procedures to ensure that the inspector properly conducted project inspections. The inspector stated that he did not always verify all of the work performed on any particular project. He also stated that he performed final inspections on projects without taking the scope of work to the sites but worked from his memory of the scope of work for certain projects.

Inadequate Monitoring

The City did not properly monitor the performance of its contractors. The inspector stated that he did not closely track the work performed by the contractors. He added that the contractors were supposed to wait for him before they closed up walls or covered roofs and that often the contractors had completed a lot of the work before he inspected the projects. The inspector noted that at times, contractors billed for the original scope of work when they had made changes. Finally, the City did not verify that the contractors employed licensed workmen to complete the rehabilitation work.

Repairs Not Received and Lack of Assurance That Funds Were Well Spent

Homeowners did not receive the repairs they were entitled to, and their lives could be at risk from substandard work. For example, in project #1621, the contractor improperly completed repairs on the electrical system by running two wires into one breaker. This error caused a current of 220 volts to run through parts of the house rather than the standard 110 volts, and there was a loss of power in other parts of the house.

The City spent more than \$1 million in Block Grant funds on 116 projects that were not completed, completed in a substandard manner, or completed at a high cost. We estimated that the City overpaid the contractors \$127,780 for projects that had work items that were either not completed or were completed in a substandard manner. In addition, for projects that had all work items completed according to contract, the City paid \$22,294 more than the completed work was worth.

Conclusion

The City had inadequate controls and did not properly spend more than \$1 million of its Block Grant Funds. It needs to collect funds paid to contractors for work not performed or work performed improperly. Additionally, we recommend that HUD require the City to develop and implement a quality control plan to ensure that all work is completed according to the scope of work.

Recommendations

We recommend that the Director of the HUD Chicago Office of Community Planning and Development require the City to

- 1A. Pursue collection of \$127,780 paid to contractors for projects in which rehabilitation work was not performed or was performed improperly.
- 1B. Require detailed inspection reports with pictures of completed repairs to ensure that all work items are properly completed according to the approved scopes of work before the contractors are paid.
- 1C. Develop and implement a postrepair quality control process to ensure that work is completed according to the scope.

Finding 2: The City Did Not Always Prepare Specific and Detailed Scopes of Work Before Contracting for Block Grant-Funded Rehabilitation Work

The City did not always prepare specific and detailed scopes of work before contracting for Block Grant-funded rehabilitation work. This condition occurred because City staff had inadequate contract management training and outdated inspection software. As a result, the City could not adequately solicit comparable bids or measure contractor performance.

The City did not always prepare specific and detailed scopes of work before contracting for Block Grant-funded rehabilitation work.

Lack of Specific and Detailed Scopes of Work

Lack of Specific Scopes of Work

The City did not always prepare scopes of work that specifically listed the work to be performed before contracting for Block Grant-funded rehabilitation work. Some of the scopes of work reviewed did not contain enough information to enable a contractor to know exactly what work was required. For example, for project #1621, part of the contract required the contractor to install a new circuit complete with hookup at panel and receptacles “as specified” and the size “as specified.” However, no specifications were listed.

Lack of Detailed Scopes of Work

The City did not always prepare scopes of work that listed the quantity of materials required or dimensions of areas in need of work before contracting for Block Grant-funded rehabilitation work. For example, for project #1409, part of the contract required the contractor to install new gutters, install underlayment and tile, and repair drywall in the bathroom. The scope of work did not specify the length of gutters to be installed or the area of the bathroom that required new underlayment and tile as well as the area requiring drywall repair.

As described above, the scopes of work did not provide enough information to determine all of the requirements for the rehabilitation work. In addition, the City did not conduct walk-throughs of the projects with the contractors to clear up any issues before accepting bids. Regulations at 24CFR 85.36(d)(2) state that a complete, adequate, and realistic specification or purchase description must be available, prior to the City advertising for bids.

Inadequate Training and Outdated Inspection Software

City staff had inadequate contract management training and outdated inspection software.

Inadequate Training

City staff had not had contract management training in more than 3 years. They last attended training relating to contracting in 2007 and had not received training relating to managing a rehabilitation program since then. In addition, the last construction training received by City staff was unrelated to work writeups. After the audit started, the City registered its staff for construction management training scheduled to cover areas such as inspections, work writeups, plans, and specifications.

The inspector did not provide dimensions of areas to be worked on to the contractors to avoid excessive change orders. He stated that if he wrongly measured the dimensions of the areas requiring repairs and put a lesser area in the scope of work, the contractors would request change orders to complete the work. We concluded that the inspector did not realize that to obtain comparable bids, he was required to provide the dimensions of the areas needing repairs to potential bidders.

Outdated Inspection Software

The inspection software version used by the inspector to produce the scopes of work was outdated and used 2001 information. The software package is menu driven and creates scopes of work once the user enters the type of work to be performed, the unit cost, and the dimensions of the areas requiring repairs. The software version installed on the inspector's computer did not generate specific details about the work items. We attempted to contact the software's maker to determine whether there was a newer version, but we were unable to do so, and its Web site had not been updated in more than 2 years.

Inability To Compare Bids and Measure Performance

As a result of the lack of detailed and specific scopes of work, the City could not adequately solicit comparable bids or measure contractor performance. Bids solicited from nonspecific and nondetailed scopes of work cannot be compared because each contractor creates bids based on its own interpretation of the scope of work, which creates wide variances in bid amounts. Additionally, scopes of work that are not detailed and specific create a hurdle for the City in measuring the performance of the contractor.

Conclusion

The City's staff had inadequate training and tools and, therefore, did not create detailed and specific scopes of work. Therefore, it could not compare bids or adequately measure contractor performance. The City needs to provide training to its staff, update its inspections software to ensure that it is more detailed, and seek technical assistance from HUD.

Recommendations

We recommend that the Director of the HUD Chicago Office of Community Planning and Development

- 2A. Require the City to provide contract management training to staff members.
- 2B. Require the City to update its inspection software to ensure that it is more detailed or use a different software package that will provide more detailed scopes of work.
- 2C. Provide technical assistance to the City in the area of contract management.

Finding 3: The City Did Not Always Follow Federal Procurement Regulations and Its Own Policy While Managing Rehabilitation Contracts

The City did not always follow Federal procurement regulations and its own policy while managing 52 of 147 rehabilitation contracts. This condition occurred because the City's internal controls were inadequate and its staff was unaware of all of the requirements. As a result, the City could not document that \$475,747 spent on these contracts was reasonable or necessary.

The City did not always follow Federal procurement regulations and its own policy while managing 52 of 147 rehabilitation contracts. Appendix C contains a schedule of the deficiencies identified in each of the 52 projects with deficiencies.

Lack of Cost Estimates for Executed Contracts

Lack of Cost Estimates for Executed Contracts

The City did not prepare cost estimates for the executed contracts or change orders for 33 of the projects reviewed. Regulations at 24 CFR 85.36(f)(1) require the City to perform a cost or price analysis in connection with every procurement action including contract modifications. Additionally, the regulations state that grantees must make independent estimates before receiving bids or proposals.

For example, for project #1691, the City processed a change order to repair water damage in a bathroom walls and floor. It did not perform and document a cost estimate for this change.

Lack of Justification for Selecting Contractors

The City did not document the justification for selecting contractors for rehabilitation contracts for 11 of the projects reviewed. Regulations at 24 CFR 85.36(b)(9) state that grantees and subgrantees will maintain records sufficient to detail the significant history of a procurement. These records will include but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price. For project #1590, the City paid off the initial contractor that started the rehabilitation work but did not complete it. It then awarded the contract to another contractor to complete the work but did not document how it selected the bid submitted by the second contractor as it was not listed on the bid review sheet. In addition, the City did not always select the lowest bidder.

Lack of Appraisals When Work Equaled or Exceeded \$10,000

The City granted 10 rehabilitation contracts that equaled or exceeded \$10,000 without obtaining appraisals for the properties. The City's policy requires appraisals for all rehabilitation projects that equal or exceed \$10,000.

Missing Rationale for Exceeding Grant Limits on Executed Contracts

The City did not document the rationale for exceeding grant limits on the executed contracts for 11 of the projects reviewed. The City's policy sets maximum levels of funding for each of the three home rehabilitation programs. For project #1604, the City spent \$15,400 to repair the home when the maximum for the emergency repair program was \$9,999. The City did not document why it paid \$5,401 more than the program limit or why it split the rehabilitation of the house into two separate contracts with different contractors.

Undocumented Change Orders

The City did not document approved change orders for the executed contracts for 15 of the projects reviewed. For project #1754, the City substituted the approved fascia, gutter, and soffit work for living room ceiling repair and insulation work without obtaining an approved change order or performing a cost estimate. However, the contractor billed for and was paid the original contract sum.

Missing Lien Waivers for Executed Contracts

The City did not obtain lien waivers for eight of the projects reviewed before paying the contractors. The City's rehabilitation procedures require the receipt of lien waivers from contractors before issuing payment.

Inadequate Internal Control and Staff Unaware of Requirements

The City's internal controls were inadequate, and its staff was unaware of all requirements.

Inadequate Internal Controls

The City did not have adequate internal controls in place to ensure compliance with Federal procurement regulations and its own procurement policy. For example, the City's change order process was lengthy, and staff circumvented it to ensure that the homeowners were not harmed by delays. The City's change order process required more levels of approval when the Community Development Department transitioned to City control in 2005. In addition, the inspector stated that he contacted contractors to obtain cost estimates for change orders, but this communication was not documented in the files. Internal controls must create an environment that ensures that the requirements are followed.

Staff Unaware of Requirements

City staff was not aware that it was violating the requirements when managing the rehabilitation program. For example, some of the staff members were not aware that appraisals were required for projects that cost \$10,000 or more. Additionally, staff was not aware of the requirements for handling projects that had substituted work items but the same invoiced amount. Specifically, the staff was not aware of the requirements for determining whether the substituted items were

comparable in cost. Finally, staff was not aware of the maximum dollar limit for change orders. Staff members must be aware of all of the requirements of their positions to ensure that limited grant funds are spent appropriately and in compliance with the requirements.

No Assurance That Costs Were Reasonable or Necessary

The City could not document that \$475,747 spent on these 52 contracts was reasonable or necessary. The City must ensure that it follows Federal procurement regulations as well as its own procurement procedures and policies to ensure that all costs incurred are reasonable and necessary in meeting its goals of providing decent and affordable housing opportunities.

Based on finding 1, 2, and 3, as well as the findings in audit report 2010- KC-1008, the City failed to properly process 146 of the 147 Block Grant home rehabilitation program projects reviewed. Regulations at 24 CFR 570.910 list actions that HUD can take to prevent a continuation of a performance deficiency, mitigate the adverse effects of a deficiency, and prevent recurrence of a deficiency. One such action is to condition the use of funds from a succeeding fiscal year's allocation upon appropriate corrective action by the recipient. The City planned to spend \$400,000 in 2010 Block Grant funding on its housing rehabilitation programs.

Conclusion

The City did not comply with Federal procurement requirements as well as its own procurement policy because it had inadequate controls in place and its staff was not aware of the requirements. Therefore, it had no assurance that the contracts awarded were reasonable or necessary. HUD needs to withhold a portion of the City's 2010 funding until it improves its controls. Additionally, the City needs to provide training to its staff and develop and implement adequate internal controls to ensure compliance with Federal procurement regulations and its own procurement policy.

Recommendations

We recommend that the Director of the HUD Chicago Office of Community Planning and Development

3A. Withhold \$400,000 in 2010 Block Grant funding for the City's housing rehabilitation programs until it improves its controls.

- 3B. Require the City to develop and implement adequate internal controls to ensure compliance with Federal procurement regulations and its own procurement policy.
- 3C. Require the City to provide staff with training on Federal procurement regulations and local procurement policies.

SCOPE AND METHODOLOGY

To accomplish our objectives, we reviewed applicable laws and regulations, interviewed City staff, and reviewed City policies and procedures.

We used reports obtained from HUD's Integrated Disbursement and Information System as background information for our review. The reports from this information system revealed that there were 364 homeowner repair projects with at least one drawdown during the 5-year period covering March 2005 through February 2010. The total funded amount for these projects was more than \$3.3 million. Specifically, we used the reports to select all homeowners that received at least \$5,000 in housing rehabilitation assistance from March 2008 through February 2010. We also selected any homeowners receiving housing rehabilitation assistance from March 2005 through February 2010 who either received assistance more than once during the 5-year period or whose name or address matched employees, elected officials, or contractors of the City. This process led to a sample of 147 projects. However, we did not rely on these data for our conclusion. All conclusions were based on additional reviews performed during the audit.

We reviewed the projects' files identified through our sample selection process to determine whether the City complied with Federal procurement laws and regulations as well as its own procedures. We also conducted physical inspections at 132 of the 147 projects in our sample. We should note that one of the projects reviewed involved 2 different contractors. For the houses inspected, we estimated the cost of the repairs performed. We prepared our cost estimates using R.S. Means Residential Repair and Remodeling Costs, Contractor's Pricing Guide for 2009, as well as Chicago area retail store flyers and Internet-based vendors' pricing. When a work item was not performed, did not meet code, or was of substandard quality and needed to be redone to have value, we estimated the cost of that work item as zero. When we were unable to verify that a work item had been completed, we gave the contractor credit for that item in our estimate. If the quantities were unknown, we used the contractor's price if it seemed reasonable. The inspections and cost estimates were performed by OIG's appraiser who is a registered architect.

Our audit period generally covered March 2008 through February 2010 and we expanded it as explained in the sample selection above. We performed our audit work onsite at the City's municipal building located at 301 River Park Drive, East St. Louis, IL, and in various assisted houses from April to November 2010.

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

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 objectives:

- Controls to ensure that Block Grant-funded housing rehabilitation contracts are completed based on the approved scopes of work.
- Controls to ensure that Block Grant-funded housing rehabilitation contracts are processed according to the applicable rules and regulations.

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 Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- The City did not have adequate controls in place to properly manage Block Grant-funded housing rehabilitation contracts.

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible 1/	Funds to be put to better use 4/
1A	\$127,780	
3A		\$400,000

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/ 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 findings 1 and 3 of this report, we concluded that the City awarded more than \$1 million in Block Grant funds for 124 rehabilitation contracts without adequately ensuring that it complied with requirements and that the work was completed in a professional manner. Because these same projects have already been questioned in our report 2010-KC-1008, issued September 28, 2010, which questioned more than \$1.2 million in Block Grant funds, we did not include these costs in the schedule of questioned costs in this report.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



From the Office of Deletra M. Hudson, City Manager

301 River Park Drive • East Saint Louis, Illinois 62201
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January 28, 2011

Mr. Ronald J. Hosking
Regional Inspector General for Audit
Region VII Office of Audit
Gateway Tower II, 5th Floor
400 State Avenue
Kansas City, KS 66101-2406

SUBJECT: The City of East St. Louis Did Not Properly Manage Housing Rehabilitation Contracts Funded by the Community Development Block Grant Program

Dear Mr. Hosking:

We recently met with two of your staff members to discuss the draft audit report prepared by your office. Per the direction from your staff, this letter contains the City's response to the three (3) Findings of non-compliance based on the above referenced subject. As stated in your report, this is the third audit on the City's Block Grant programs, and more specifically, this is the second audit on this sampling of the rehabilitation files.

Previously, the City did state that while all of our files did not contain all of the proper documentation per HUD's regulations and requirements, we did have the documentation in our office and/or at our disposal for the majority of the cases. Since that phase of the audit, we have added the additional documentation to our files to ensure compliancy and complete the files.

The City strives to properly manage all of our federally-funded programs and to ensure compliance with all of the Code of Federal Regulations. In doing so, the City is aware that improvements can always be made to enhance our internal controls and increase our performance levels. Therefore, the City of East St. Louis does not agree with the Findings revealed in this third audit. The following provides a summary of our response to this audit report:

Finding #1 - Disagree

Internal discussions and monitoring discovered that there was some inconsistency with specific work write-ups and controls over the contracting process. Those issues have already been addressed and corrected. Specific work write-ups are prepared for all rehabilitation projects and photos documenting before and after the rehabilitation work will be taken to ensure that all work items are properly completed according to the approved scopes of work prior to contractors receiving payment.

Finding #2 - Disagree

Contrary to the audit Finding, a newer version of the inspection software system was installed for the inspector; however, technical difficulties and software support problems prevented the newer version from operating to its full capacity. Consequently, the older version overrode the newer one. We are

Comment 1

Comment 2

Ref to OIG Evaluation

Auditee Comments

Comment 3

Mr. Hosking, page 2

currently sampling two (2) new software systems, one of which will be purchased and installed before any new housing rehabilitation projects are started.

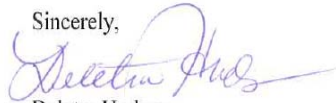
Finding #3 - Disagree

Although contract changes that did not affect the monetary value of the contract were documented in the file, we understand the concern and the need to ensure that contract modifications are properly documented and justified through cost analysis, contractor selections and change orders. Prior to this audit, the City began requiring cost analysis for all change orders. We are also developing a new internal form for non-monetary changes to properly document the authorization of these changes and to accompany the file.

Additionally, some of our staff members have already attended contract management training sessions, and we will make sure that all of our staff members attend job-related training classes as they become available.

As always we welcome technical assistance and support from HUD, and we will also work directly with HUD's staff to provide any additional information required. If you have any questions, please contact me at 618-482-6785 or Carla Harris, Interim Community Development Director, at 618-482-6672.

Sincerely,



Deletra Hudson
City Manager

OIG Evaluation of Auditee Comments

- Comment 1** While the City might have noted inconsistencies with specific work write-ups and controls over the contracting process, it did not provide the OIG with documents to show that these were rectified. The City stated that it will be requiring inspection photos for rehabilitation projects before and after completion of the work. This should help in verifying that the work is completed according to the approved scope of work.
- Comment 2** The City was aware of the problems with its inspection software and therefore could not have obtained the best work write-ups during the audit period. The City stated that it is seeking alternative software packages. We expect it to implement a new inspection system before initiating any new rehabilitation projects.
- Comment 3** The City could not prove that these contract changes would have caused the monetary values of the contracts to remain unaffected since it did not follow all the procurement requirements in 24CFR85.36. In addition, the City did not provide documentation to the OIG during the audit to support the fact that it was requiring cost analyses for all change orders. The City stated that it is developing a new form to document the approval of contract changes that do not affect the original contract amount and providing its staff with contract management training. These actions should help address some of our recommendations.

Appendix C

SCHEDULE OF DEFICIENCIES

#	IDIS* #	Amount paid	Work items not performed	Work items not properly performed	Cost not reasonable	When cost not reasonable, difference between contract price and OIG estimate	Failure to document a cost estimate	Contract granted without competition	Lowest bid not selected	Lack of appraisal	Grant amount exceeded	Missing change order	Missing lien waivers
1	1409	\$4,938		x	x	\$284	x					x	x
2	1433	\$4,850		x	x	\$4,043							
3	1458	\$4,650		x									
4	1499	\$4,050					x						
5	1502	\$4,463		x	x	\$961							
6	1521	\$4,700	x	x					x				
7	1535	\$5,200			x	\$357	x		x				
8	1540	\$4,500	x	x	x	\$2,605							x
9	1546	\$8,550		x	x	\$1,640	x				x		
10	1550	\$5,985		x	x	\$3,573	x						
11	1556	\$9,800		x			x						
12	1569	\$5,257		x	x	\$986							
13	1572	\$9,000		x									
14	1573	\$13,750	x	x									
15	1574	\$14,650		x									
16	1575	\$8,950	x		x	\$1,154							
17	1576	\$7,500	x	x	x	\$279	x						x
18	1577	\$10,000		x	x	\$648				x	x		
19	1579	\$7,315	x		x	\$2,168							
20	1581	\$9,000		x									
21	1586	\$10,000			x	\$752				x	x		
22	1587	\$8,600		x	x	\$37							
23	1588	\$6,033	x		x	\$1,173		x					
24	1589	\$9,950		x	x	\$695							

#	IDIS* #	Amount paid	Work items not performed	Work items not properly performed	Cost not reasonable	When cost not reasonable, difference between contract price and OIG estimate	Failure to document a cost estimate	Contract granted without competition	Lowest bid not selected	Lack of appraisal	Grant amount exceeded	Missing change order	Missing lien waivers
25	1590	\$15,390						x		x	x		x
26	1591	\$8,900			x	\$2,224							
27	1592	\$9,925	x	x	x	\$878	x					x	
28	1593	\$5,000		x									
29	1596	\$9,325		x	x	\$1,592							
30	1597	\$9,400	x	x	x	\$533							
31	1598	\$4,950	x	x	x	\$1,181	x					x	
32	1604	\$15,400		x	x	\$2,489		x		x	x		
33	1605	\$7,630			x	\$1,747			x				
34	1606	\$8,800		x									
35	1607	\$8,752		x	x	\$1,732							
36	1609	\$7,070			x	\$925							
37	1610	\$8,650		x									
38	1618	\$7,200		x	x	\$2,054							
39	1619	\$6,000		x									
40	1621	\$5,525		x	x	\$962							x
41	1665	\$9,300		x	x	\$2,080							
42	1666	\$7,100	x	x	x	\$198							
43	1668	\$7,100		x	x	\$2,756							
44	1669	\$9,425		x	x	\$1,612							
45	1670	\$9,400	x	x	x	\$3,014							
46	1671	\$5,000	x		x	\$3,456							
47	1672	\$8,055	x	x									
48	1673	\$5,600		x									
49	1674	\$9,950		x									
50	1675	\$9,600		x	x	\$4,553							
51	1680	\$9,000			x	\$3,623							
52	1681	\$7,300	x	x	x	\$2,457							
53	1683	\$7,700		x	x	\$2,271							

#	IDIS* #	Amount paid	Work items not performed	Work items not properly performed	Cost not reasonable	When cost not reasonable, difference between contract price and OIG estimate	Failure to document a cost estimate	Contract granted without competition	Lowest bid not selected	Lack of appraisal	Grant amount exceeded	Missing change order	Missing lien waivers
54	1685	\$9,700	x	x	x	\$1,943	x					x	
55	1686	\$6,800			x	\$5,951							
56	1687	\$9,895		x	x	\$816							
57	1688	\$9,900		x	x	\$900	x						
58	1689	\$13,162						x			x		
59	1690	\$9,200		x									
60	1691	\$9,975		x	x	\$1,820	x					x	
61	1692	\$6,500	x	x	x	\$2,260							
62	1693	\$9,150		x									
63	1694	\$9,400		x			x					x	
64	1695	\$9,999			x	\$65							
65	1697	\$9,500		x	x	\$106							
66	1698	\$6,820	x	x	x	\$1,390							
67	1699	\$7,250		x	x	\$2,343							
68	1701	\$9,500	x	x	x	\$1,073	x	x					
69	1702	\$8,100		x									
70	1709	\$9,800		x	x	\$2,003	x						
71	1711	\$9,500		x	x	\$1,917							
72	1713	\$9,995	x	x	x	\$596							
73	1714	\$8,650		x	x	\$494							
74	1715	\$9,220	x	x	x	\$2,283							
75	1717	\$8,150		x									
76	1719	\$7,800		x	x	\$2,909							
77	1720	\$10,000								x		x	
78	1721	\$9,950	x	x	x	\$3,158	x					x	
79	1722	\$10,400	x	x	x	\$2,438				x			
80	1724	\$8,840		x	x	\$54							
81	1726	\$9,980		x	x	\$1,518						x	
82	1727	\$7,950		x	x	\$885							

#	IDIS* #	Amount paid	Work items not performed	Work items not properly performed	Cost not reasonable	When cost not reasonable, difference between contract price and OIG estimate	Failure to document a cost estimate	Contract granted without competition	Lowest bid not selected	Lack of appraisal	Grant amount exceeded	Missing change order	Missing lien waivers
83	1728	\$10,000					x			x	x	x	
84	1731	\$8,500		x									
85	1732	\$4,895		x	x	\$249							x
86	1739	\$1,900		x	x	\$1,633							
87	1740	\$14,710		x									
88	1741	\$15,610		x				x			x		
89	1742	\$13,135	x	x	x	\$2,908				x			
90	1743	\$9,200					x					x	
91	1744	\$12,740	x	x	x	\$3,241				x			
92	1745	\$9,500		x	x	\$1,975	x		x				
93	1746	\$9,400		x	x	\$2,570							
94	1747	\$8,900					x						
95	1749	\$9,250		x	x	\$3,835							x
96	1750	\$12,300			x	\$2,006	x						x
97	1751	\$12,994			x	\$1,274							
98	1752	\$6,900		x			x						
99	1753	\$6,800					x						
100	1754	\$9,700		x	x	\$586	x					x	
101	1757	\$7,725		x	x	\$3,135							
102	1758	\$8,800		x									
103	1769	\$9,875		x			x						
104	1770	\$2,379			x	\$984							
105	1776	\$9,300	x		x	\$508							
106	1777	\$8,800		x	x	\$1,316							
107	1778	\$7,600		x									
108	1783	\$7,635	x	x									
109	1805	\$8,900		x									
110	1811	\$8,850	x	x	x	\$1,828							
111	1816	\$13,600		x	x	\$666							

#	IDIS* #	Amount paid	Work items not performed	Work items not properly performed	Cost not reasonable	When cost not reasonable, difference between contract price and OIG estimate	Failure to document a cost estimate	Contract granted without competition	Lowest bid not selected	Lack of appraisal	Grant amount exceeded	Missing change order	Missing lien waivers	
112	1823	\$10,025		x	x	\$602					x			
113	1824	\$9,850		x			x							
114	1827	\$6,715		x										
115	1830	\$10,000		x			x				x			
116	1832	\$9,350		x	x	\$5,453								
117	1833	\$8,720		x	x	\$1,887	x							
118	1834	\$9,975		x	x	\$3,205	x					x		
119	1836	\$7,520	x	x	x	\$2,805	x					x		
120	1837	\$8,500		x	x	\$309								
121	1838	\$9,100		x	x	\$2,044	x							
122	1839	\$10,000			x	\$2,386	x		x	x	x	x		
123	1842	\$9,400		x	x	\$2,056								
124	1843	\$9,909	x	x			x							
		\$1,078,185	30	99	84	\$150,074	33	6	5	10	11	15	8	

* IDIS = Integrated Disbursement and Information System

Appendix D

CRITERIA

Code of Federal Regulations

Regulations at 24 CFR 85.36(b)(2) state that grantees and subgrantees will maintain a contract administration system which ensures that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders.

Regulations at 24 CFR 85.36(b)(9) state that grantees and subgrantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

Regulations at 24 CFR 85.36(c)(3)(i) state that grantees will have written selection procedures for procurement transactions. These procedures will ensure that all solicitations incorporate a clear and accurate description of the technical requirements for the material, product, or service to be procured.

Regulations at 24 CFR 85.36(d)(2), Procurement by sealed bids (formal advertising), state that bids are publicly solicited and a firm-fixed-price contract (lump sum or unit price) is awarded to the responsible bidder whose bid, conforming with all the material terms and conditions of the invitation for bids, is the lowest in price. The sealed bid method is the preferred method for procuring construction, if the conditions in §85.36(d)(2)(i) apply.

In order for sealed bidding to be feasible, the following conditions should be present:

1. A complete, adequate, and realistic specification or purchase description is available;
2. Two or more responsible bidders are willing and able to compete effectively and for the business; and
3. The procurement lends itself to a firm fixed price contract and the selection of the successful bidder can be made principally on the basis of price.”

Regulations at 24 CFR 85.36(f)(1) state that grantees and subgrantees must perform a cost or price analysis in connection with every procurement action including contract modifications. The method and degree of analysis is dependent on the facts surrounding the particular procurement situation, but as a starting point, grantees must make independent estimates before receiving bids or proposals. A cost analysis must be performed when the offerer is required to submit the elements of his estimated cost, e.g., under professional consulting, and architectural engineering services contracts. A cost analysis will be necessary when adequate price competition is lacking, and for sole source procurements, including contract modifications or change orders, unless price reasonableness can be established on the basis of a catalog or market price on a commercial product sold in substantial quantities to the general public or based on prices set by law or regulation. A price analysis will be used in all other instances to determine the reasonableness of the proposed contract price.

Regulations at 24 CFR 570.202(a)(1) state that Block Grant funds may be used to finance the rehabilitation of privately owned buildings and improvements for residential purposes.

Regulations at 24 CFR 570.910(b)(8) state that in the case of an entitlement recipient, [HUD can] condition the use of funds from a succeeding fiscal year's allocation upon appropriate corrective action by the recipient pursuant to section 570.304(d). The failure of the recipient to undertake the actions specified in the condition may result in a reduction, pursuant to section 570.911, of the entitlement recipient's annual grant by up to the amount conditionally granted.

Regulations at 2 CFR 225(c)(2), state that a cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The question of reasonableness is particularly important when governmental units or components are predominately federally-funded. In determining reasonableness of a given cost, consideration shall be given to:

- a. Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the governmental unit or the performance of the Federal award.
- b. The restraints or requirements imposed by such factors as: sound business practices; arms length bargaining; Federal, State and other laws and regulations; and, terms and conditions of the Federal award.
- c. Market prices for comparable goods or services.
- d. Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the governmental unit, its employees, the public at large, and the Federal Government.
- e. Significant deviations from the established practices of the governmental unit which may unjustifiably increase the Federal award's cost.

City Criteria

COST ESTIMATE AT OR BELOW GRANT LIMIT

If the estimate is within a reasonable range of the grant maximum (which is defined as a maximum of \$15,000.00 – Home Repair/Lottery, \$9,999 – Senior Repair and Emergency Repair, and \$25,000 – HOME Rehab/Lead Reduction) for rehabilitation repairs the work write-up is sent for bids to licensed contractors.

COST ESTIMATE ABOVE GRANT LIMIT

If the bid estimate is in excess of the grant maximum \$15,000.00 – Home Repair/Lottery, \$9,999 – Senior Repair and Emergency Repair, and \$25,000 – HOME Rehab/Lead Reduction for rehabilitation work, the following actions can be taken:

1. The homeowner is contacted to determine if they have any resources to fund the contracts cost over the grant maximum.

2.
 - A. If the applicant does not have the resources, the inspector can delete some line items from the work write-up to bring the cost estimate down if feasible. If it is found not to be feasible, it must be denied and the applicant must be notified in writing as the home cannot be rehabilitated within the grant limit guidelines.
 - B. When using HOME funds, the reason for denial is that the home must be brought up completely to code under the City’s adopted International Code Council within the program’s financial guidelines, and the anticipated rehabilitation costs exceed these program limits.
 - C. The home may also be denied when the Inspector deems that the home is structurally unsound and cannot be rehabilitated.

3. After the bid period has expired, the lowest responsible bidder (from the Community Development Department approved Contractor List) is awarded the contract. Generally the lowest bid is within 20% of the Community Development Department cost estimate.

APPRAISALS

Property appraisals to determine the before-rehab value and the after-rehab value may be required for Community Development rehabilitation programs based on the following:

1. A property appraisal is required for ALL rehabilitation projects funded through HOME programs. A real estate office/appraisal agent is contracted to conduct both appraisals (before and after rehab).

2. If CDBG [Block Grant] funds are used to complete the home repair work, a property appraisal is required if the contract value is \$10,000 or greater. A real estate office/appraisal agent is contracted to conduct both appraisals (before and after rehab).

CONTRACT COMPLETION

1. A contract is then written and signed by the Contractor and Community Development Department for the amount of the award with all relevant Community Development regulations incorporated.
2. A written Notice to Proceed is issued and the Contractor proceeds with the rehabilitation work for the project at this time.
3. The Community Development Inspector makes site progress inspections to monitor the project. The Inspector is to prepare written inspection reports and photograph the work-in-progress for Community Development Department files.
4. The Inspector also advises contractors if any deficiencies occur or if any corrections have to be made during the job's progress and he ensures that proper action is taken. If corrections are required that were not included in of the original scope of work, a Change Order is required. (Change orders must be submitted in writing by the Housing Inspector to the Community Development Director, City Manager, Budget Director, Finance Director and Financial Advisory Authority for approval.)

PAYMENTS

1. One payment is made to the Contractor upon completion of the entire project. The payment process includes the approval of the Community Development Housing Inspector and Program Manager as well as the Property Owner.
2. For any jobs containing lead hazard reductions, a clearance must be achieved by a licensed lead risk assessor before any payment is made to the contractor. Upon the completion of the rehabilitation, the Housing Inspector conducts a final inspection. If all work meets the work write-up job specifications and contract requirements, the contractor's payout request is initiated.
3. Contractor must submit executed Lien Waiver and Invoice before Final payout is made.