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Audit Report Number  
2007-BO-1005

TO: Robert Paquin, Director, Office of Community Planning and Development,  
Boston Regional Office, 1AD

FROM:   
John Dvorak, Regional Inspector General for Audit, 1AGA

SUBJECT: The City of New Bedford, Massachusetts, Did Not Meet Certain Requirements  
of HUD's Community Development Block Grant Program

## **HIGHLIGHTS**

### **What We Audited and Why**

As part of our annual plan, we audited the Office of Housing and Community Development, City of New Bedford, Massachusetts' (City) administration of its Community Development Block Grant (CDBG) and HOME Investment Partnerships (HOME) programs. Our audit objective was to determine whether the City complied with U.S. Department of Housing and Urban Development (HUD) regulations in administering its CDBG and HOME programs.

### **What We Found**

The City generally administered its CDBG and HOME programs in accordance with HUD regulations. However, it did not always ensure that its subrecipients followed HUD requirements or met the program objectives of the subrecipient

agreements. The City failed to ensure that two of its subrecipients followed HUD requirements for full and open competition regarding procurements for construction work. It also did not ensure that another subrecipient attained its program objectives of issuing the required number of loans and creating the required number of new jobs. In addition, the City did not ensure that this subrecipient properly collateralized CDBG funds on deposit in the same bank, or made loans that did not involve conflicts of interest. These problems occurred because the City did not always adequately monitor subrecipient activities or failed to ensure that its subrecipients always took corrective action. As a result, there is a lack of assurance that subrecipient procurements were fair and equitable and that the most favorable contract prices were obtained for \$750,000 in construction funding. Also, more than \$1 million in CDBG funding for loans and job creation may not have been the best use of HUD funds, CDBG funds totaling \$188,177 were not adequately safeguarded against loss, and a subrecipient approved two loans that created apparent conflicts of interest.

### **What We Recommend**

We recommend that the director of the Office of Community Planning and Development in Boston require the City to (1) obtain a cost analysis for each subrecipient to support the \$750,000 in CDBG funding provided for construction contracts, (2) ensure that the future use of CDBG funds creates the number of new jobs necessary to fulfill the requirements of past and current agreements to put current funding of \$285,000 to better use, (3) obtain and provide evidence that CDBG funds in excess of Federal Deposit Insurance Corporation (FDIC) limits for the subrecipient are fully collateralized, and (4) ensure that the subrecipient establishes adequate policies addressing conflicts of interest including requirements for providing full disclosure.

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

### **Auditee's Response**

We provided City officials with a draft audit report on March 21, 2007, and requested a response by April 4, 2007. We held an exit conference with City officials on March 29, 2007, to discuss the draft report, and we received their written comments on April 4, 2007. The City generally agreed with the facts,

conclusions and recommendations in Findings 2, 3 and 4 of this report. The City partially agreed with certain comments and conclusions contained in Finding 1.

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 OBJECTIVES

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The City of New Bedford, Massachusetts (City), receives annual Community Development Block Grant (CDBG) program funds from the U.S. Department of Housing and Urban Development's (HUD) Office of Community Planning and Development. The CDBG program is a flexible program that provides communities with resources to address a wide range of unique community development needs. The City also receives HUD funding from the HOME Investment Partnerships program (HOME) and the Emergency Shelter Grant program and competitive funding from the Supportive Housing program. The City's Office of Housing and Community Development receives HUD funding on behalf of the City. The Office of Housing and Community Development engages residents, nonprofit organizations, developers, and the general public in articulating the office's needs and priorities for expanding the stock of safe, decent, and affordable housing; stimulating economic development; supporting programs and services for community development; and revitalizing neighborhoods.

The CDBG and HOME programs are the primary sources of HUD income for the Office of Housing and Community Development. From 2003 through 2005, the office received more than \$10.6 million in CDBG funds and \$4.2 million in HOME funds. A primary requirement of the CDBG program is that activities and/or services funded under the program meet one of three national objectives. These objectives include activities that (1) benefit low-to-moderate-income persons, (2) aid in the prevention or elimination of slums or blight, or (3) are designed to meet community development needs having a particular urgency.

HOME is the largest federal block grant provided to state and local governments designed exclusively to create affordable housing for low-income households. HOME provides formula grants to states and localities that communities use—often in partnership with local nonprofit groups—to fund a wide range of activities that build, buy, and/or rehabilitate affordable housing for rent or homeownership or provide direct rental assistance to low-income people.

In addition to its public service subgrantees (subrecipients), the City's Office of Housing and Community Development has four economic development subrecipients. The largest of these is the New Bedford Economic Development Council (Council), which is responsible for most of the economic development in the City. The Council has acted as a catalyst for the City's economic development growth by working with various local constituent groups to attract new businesses and job opportunities and to improve the quality of life for City residents. In the Council's subrecipient agreements with the Office of Housing and Community Development, it received more than \$1 million in HUD funds for program years 2003, 2004, and 2005 as a supplement to the salaries of staff members who process and monitor loan programs. One of the primary requirements under these agreements is to use the Community Economic Loan Fund (CDBG entitlement), Micro-Enterprise Loan Fund (CDBG entitlement), Fishing Industry Revolving Loan Fund (grants available from the U. S. Economic Development Administration [EDA]), and other funds to make loans available to qualifying firms and micro-businesses to create new jobs in the City. As a condition of accepting the loans, the assisted businesses must agree to submit quarterly job creation information.

Our audit objective was to determine whether the City's Office of Housing and Community Development complied with HUD regulations in the administration of its CDBG and HOME programs, including whether (1) the City had effective safeguards over HUD funds; (2) a subrecipient, the Council, met specific program objectives of its agreements with the City, regarding the number of loans to be issued and the number of new jobs to be created, and whether job creation documentation provided by the Council met the requirements of the subrecipient agreements, and 3) there were any conflict-of-interest issues relative to economic development loans.

## RESULTS OF AUDIT

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### Finding 1: The City Did Not Ensure That Its Subrecipients Followed HUD Regulations in Their Procurement Processes

The City did not ensure that two of its subrecipients followed HUD requirements for full and open competition for their construction work procurements. For one of the subrecipients, the independent cost estimate prepared before the receipt of bids or proposals was inadequate and did not ensure that rehabilitation costs were reasonable. In addition, both subrecipients improperly proceeded with the procurements, despite an inadequate response to their solicitations, and failed to prepare the necessary cost analyses when adequate price competition was lacking. These deficiencies occurred because the City did not maintain an effective system of controls to adequately monitor the subrecipients' procurement and contracting processes. As a result, there is a lack of assurance that the procurement process was fair and equitable and that the most favorable contract prices were obtained for \$750,000 in CDBG funding provided for the construction work.

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#### **The First Subrecipient's Independent Cost Estimate Was Inadequate**

The first subrecipient did not follow proper procedures before awarding its procurement noncompetitively. The work under the contract involved the first phase of a planned restoration and renovation of the subrecipient's operations.<sup>1</sup> However, the independent cost estimate for this procurement was inadequate and had limited usefulness in ensuring that rehabilitation costs were reasonable. The cost estimate of \$802,616 submitted by the owner's architect pertained to the overall restoration and renovation of the subrecipient's operation and was based on a preliminary scope of work. Although the first phase work was reportedly included in this estimate, the estimate did not specifically identify costs for the first phase. We contacted the architect to obtain the basis for the first phase's estimated costs included in the architect's written bid assessment (dated February 22, 2005) because we could not reconcile certain written assessment costs to the overall estimate. However, the architect failed to provide us the requested information. A separate cost estimate should have been performed for the first phase construction work.

The director of the City's Office of Housing and Community Development informed us on February 9, 2007 that the first phase cost estimate prepared by the owner's architect totaled \$365,272 and represented roof repairs, gutters, down

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<sup>1</sup> The City committed \$250,000 for the first phase and did not provide any funding beyond the first phase.

spouts, chimney repairs, dormer repair, and replacement of the roof balustrade. The director further stated that this cost estimate was reflective of the work included in the invitation to bid. However, the cost estimate was not completely reflective of what was included in the invitation to bid or the bid submitted by the sole bidder. The invitation to bid and the bid submitted by the sole bidder included additional cost items, such as front porch repairs, painting, and masonry pointing that were not included in the cost estimate, as described by the City's director on February 9, 2007. In addition, the director noted that the base bid of \$339,525 from the contractor (sole bidder), referred to in the architect's written assessment of that bid, was below the architect's estimate of \$365,272. However, we do not consider this a fair comparison because the cost estimate included additional costs associated with the reconstruction of the roof balustrade that were not included in the base bid of \$339,525. Based on these inconsistencies, we believe that the owner's architect should have prepared a revised cost estimate to better reflect the scope of work. The City's director agreed that that the owner's architect should have completed a second cost estimate.

The second subrecipient did follow proper procedures in developing a cost estimate for construction of a two-level building. The architect's estimate conformed to the contract and bid quotation. Also, the bid of \$1,026,000 submitted by the sole bidder was below the subrecipient's cost estimate of \$1,178,061. The job specifications clearly detail the scope of work to be performed and the quantity of materials to be used.

### **Subrecipients Were Awarded Contracts without Full and Open Competition**

Both subrecipients improperly proceeded with the procurements for construction contracts without adequate responses to their solicitations. The contracts awarded totaled \$491,825 (first subrecipient) and \$1,026,000 (second subrecipient), which included HUD funding of \$250,000 and \$500,000, respectively. These procurements were properly advertised, but in both instances, the subrecipients received only one bid and awarded the contracts to the sole bidder. For example, the first subrecipient's register of bid documents demonstrates that eight contractors requested bid packages on the project and paid the \$50 bid deposit, but only one bid was received. The work under the solicitation involved the first phase of a planned restoration and renovation of the subrecipient's operations. The subrecipient's decision to advertise the procurement in only the local newspaper may have limited the number of responsive bidders.

The second subrecipient also did not follow proper procedures when it awarded a contract to the sole bidder for construction of a two-level building. The City reported that the subrecipient placed telephone calls to the five potential bidders in addition to a public advertisement to determine whether the contractors were



interested in bidding on the project. The subrecipient's architect also reportedly contacted two companies in the Boston, Massachusetts, area and left messages. However, there was no evidence to substantiate these claims.

HUD requires that for sealed bidding to be feasible, two or more responsible bidders must be willing and able to compete effectively for the business. Since only one bid was received for each of the procurements, it would have been prudent to readvertise the procurements to ensure that contracts were awarded in a maximum open and fair competitive manner in accordance with federal regulations. If the additional advertising failed to provide more than one bid, the City should have obtained a waiver from HUD to allow the contracts to be awarded noncompetitively.

For contracts awarded through noncompetitive proposals, the subrecipient must show that another method of procurement was not feasible because either (1) the item or service was available from a single sole source, (2) an emergency existed precluding the use of competitive solicitation, (3) HUD had authorized awarding the procurements through noncompetitive proposals, or (4) after solicitation from a number of sources, competition was determined inadequate. Since none of these conditions was sufficiently met, the procurements should not have been awarded through noncompetitive proposals.

### **Subrecipients Failed to Perform Cost Analysis**

Both subrecipients failed to perform a cost analysis. A cost analysis of bids received was necessary for the subrecipients to ensure that construction costs were reasonable, since adequate competition was lacking. Although the independent cost estimate received by the second subrecipient appeared adequate, there is a distinction between a cost estimate and a cost analysis. A cost estimate is based on historical costs, and is prepared before receiving bids or proposals. A cost analysis is performed on current price information and cost projections, and usually occurs after a bid or proposal has been received. The cost analyses were not completed in these instances because the City did not adequately enforce HUD procurement requirements.

### **Conclusion**

The subrecipients were required to promote full and open competition for all procurements to include preparing a proper cost estimate for each procurement before receiving bids or proposals. In addition, the subrecipients needed to perform a cost analysis when adequate price competition was lacking in

accordance with HUD regulations. Because the City did not ensure that the above requirements were met, it does not have complete assurance that the lowest possible prices were obtained for these contracts. These deficiencies occurred because the City did not maintain an effective system of controls, including adequate monitoring, over the subrecipients' procurement and contracting processes. As a result of these deficiencies, the City cannot support that the costs for the \$750,000 in CDBG funded contracts were reasonable.

## Recommendations

We recommend that the director of the Office of Community Planning and Development in Boston require the City to:

- 1A. Ensure that subrecipients comply with HUD requirements that bids be solicited from an adequate number of contractors and awards be made to the lowest responsive bidder.
- 1B. Ensure that subrecipients maintain adequate support showing that the cost analyses were performed and the basis used to determine the reasonability of the contracted amounts.
- 1C. Obtain a cost analysis for each subrecipient to support the \$750,000 in CDBG funding provided for construction costs.
- 1D. Provide technical assistance to ensure that the subrecipients follow procurement regulations.

## RESULTS OF AUDIT

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### Finding 2: The City Did Not Ensure That Its Subrecipient Met Requirements for Number of Loans Issued and Number of Jobs Created

The City did not ensure that a subrecipient, the New Bedford Economic Development Council (Council), met the program objectives of its subrecipient agreements for issuing the required number of loans and creating the required number of new jobs. In addition, the City did not ensure that the Council satisfied all of the quarterly reporting requirements for job creation as provided in the subrecipient agreements. These deficiencies occurred because the City did not enforce the terms of the agreements and did not provide adequate monitoring over the quarterly reporting for jobs created. As a result, CDBG funding of more than \$1 million provided to the Council over a three-year period may not have been the best use of HUD funds. Also, without comprehensive reporting, the City cannot be assured that a net gain in jobs is being achieved.

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#### **The Council Failed to Issue the Loans or Create the New Jobs Required**

The City provided the Council \$1,050,000 in CDBG funds to administer a loan program over a three-year period (\$350,000 in fiscal year 2003, \$350,000 in fiscal year 2004, and \$350,000 in fiscal year 2005). Two of the primary objectives under this program were to provide loans to eligible companies and/or micro-enterprises and to create new jobs through these loans.

From fiscal year 2003 through fiscal year 2005, the Council failed to issue the required number of loans and create the required number of new jobs. Based on the memorandums of agreement, employee income certifications, and other documentation, the results attained were below the goals of 12 loans issued and 20 new jobs created for each year as shown in the program objectives of the subrecipient agreements. The Council issued only 10 loans in 2003, nine loans in 2004, and 11 loans in 2005 for a total of 30 of the required 36 loans. Also, the Council created only 39 new jobs—16 new jobs in 2003, five new jobs in 2004, and 18 new jobs in 2005—through 15 of those 30 loans. Although the Council retained 31 existing jobs through an additional three of the 30 loans, it did not meet the primary objective of creating 60 new jobs. The remaining 12 of the 30 loans consisted of 11 micro-enterprise loans and one area benefit loan (see appendix C).<sup>2</sup>

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<sup>2</sup> For micro-enterprise businesses, no job creation documentation is necessary if the owner is a low- or moderate-income person. For area benefit loans, no job creation documentation is necessary if the business is available to all residents in a particular area, where at least 51 percent of the residents are of low and moderate income.

The Council had little difficulty in issuing the required number of loans and creating the required number of jobs before fiscal year 2003. However, the City did not take immediate action after the Council failed to achieve its goals for loans issued and new jobs created in fiscal year 2003. It continued to provide funding to the Council for three additional years (2004 to 2006) despite the Council's failure to meet the goals of the subrecipient agreements in each of the previous years (2003 to 2005). The Council did perform some outreach efforts to market its loan programs and search out businesses to create new jobs; however, these efforts were short of the goals stated in the written agreements with the City.

### **The City's Quarterly Reporting Requirements Were Not Satisfied**

The Council was required to provide the City information on jobs created and/or retained on a quarterly basis. With the exception of the quarterly labor status reports, the Council satisfied all of the City's quarterly reporting requirements for monitoring job creation/retention initiatives. The quarterly labor status reports provide information to identify jobs created or retained for businesses receiving funds from the Council and distinguish new jobs and new hires from those already in existence. However, the businesses that received loans from the Council for the purpose of creating and/or retaining jobs either did not submit the required reports to the Council or did not submit them in a timely manner.

Of the 18 businesses reported by the City as creating and/or retaining jobs over the three-year period, 10 businesses either had not submitted reports or had not done so in a timely manner. The delinquent reports were generally dated well past the reporting period. Another business had submitted an undated report, and two businesses had submitted the required reports, while the five remaining businesses were not required to submit reports due to the limited timeframe between date of loan issuance and final report date (see appendix D).

These reports are the primary mechanism that the Council used to monitor job creation and to ensure that workers were being hired for new positions rather than vacated positions. The hiring of new employees does not necessarily equate to a net gain in the number of full-time permanent employees because the business may have had turnover in existing jobs. The report requirements include reporting the number of employees of the business at the commencement of the loan and the number of employees at the beginning of each quarterly reporting period and the number of full-time/part-time jobs created each quarter be updated. This will provide assurance to the Council and the City that the businesses are creating new jobs rather than filling vacated positions.

## Conclusion

The CDBG funding of more than \$1 million that the City provided to the Council may not have been the best use of HUD funds because the Council failed to achieve its goals for the creation of new jobs and the number of loans issued. Also, without the submission of the quarterly labor status reports or their submission in a timely manner, the Council and the City cannot adequately evaluate whether a net gain in jobs has been achieved. These deficiencies occurred because the City did not enforce the terms of the subrecipient agreements and did not provide adequate monitoring over the quarterly reporting of jobs created. The Council advised the Office of the Inspector General (OIG) that it will take steps to improve its reporting. In addition, the City needs to improve its oversight to ensure comprehensive reporting.

## Recommendations

We recommend that the director of the Office of Community Planning and Development in Boston require the City to

- 2A. Ensure that the Council uses future CDBG funds to create the number of new jobs necessary to fulfill the requirements of past and current agreements to put current funding of \$285,000 to better use.
- 2B. Consider imposing sanctions or cease funding the Council should the Council fail to fulfill the requirements of past and current subrecipient agreements.
- 2C. Ensure that the Council continues its outreach efforts to market its loan programs and to attract new businesses with the purpose of creating new jobs.
- 2D. Improve its control structure to ensure that the Council properly submits the quarterly labor status reports.

## RESULTS OF AUDIT

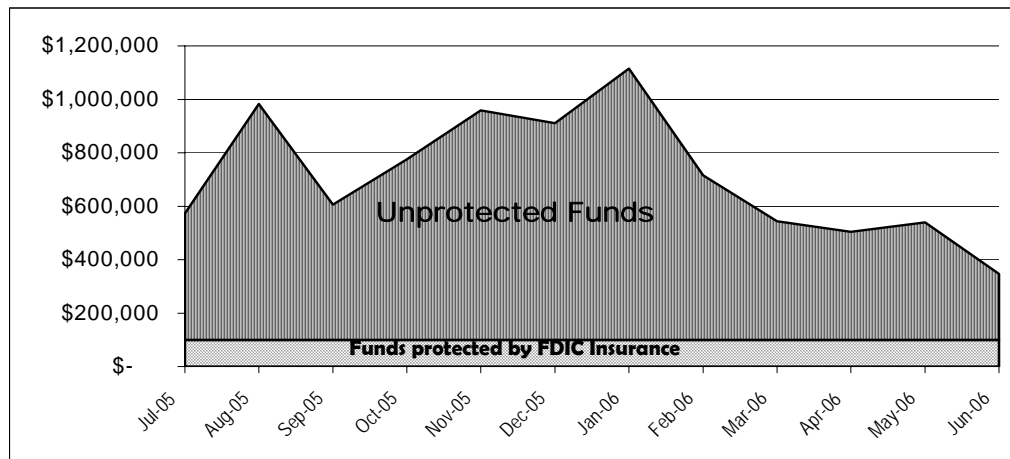
### Finding 3: The City Did Not Ensure That Its Subrecipient Properly Collateralized HUD Funds on Deposit in Excess of FDIC Limits

The City did not ensure that a subrecipient, the New Bedford Economic Development Council (Council), properly collateralized HUD funds in excess of the Federal Deposit Insurance Corporation (FDIC) limits. This occurred because the City did not take into account all of the federally provided funds on deposit by the Council in the same bank and reviewed only CDBG accounts which at year end were below the FDIC limit. As a result, \$188,177 in CDBG funds was not protected against loss in case of a bank failure.

#### Federal Funds in the Aggregate Were Not Protected Against Loss

According to FDIC regulations, depositors are protected against the loss of their insured deposits if an FDIC-insured bank fails. If a depositor's accounts at an FDIC-insured bank are less than or equal to \$100,000, the funds are fully insured. When deposits exceed the FDIC insurance limit of \$100,000, the depositor must request that the bank pledge eligible collateral to secure the uninsured amount.

As of January 2006, the Council had 10 separate federal checking accounts at Slade's Ferry bank, totaling \$1,014,624. The month of January 2006 was the highest month-end balance from July 2005 through June 2006. Of this total, \$914,624 (with \$100,000 insured by the FDIC) was not secured and, therefore, not protected against loss (see appendix E). For the 12-month period ending June 30, 2006, uninsured funds in the aggregate exceeded FDIC limits every month. Month-end balances in excess of FDIC limits ranged from a high of \$914,624 to a low of \$147,329.



Although the Council's staff noted that they were aware the assets were not fully insured, the Council made only limited efforts to correct the cited deficiency and establish a proper method to collateralize the funds. In addition, the City monitored the CBDG funds on deposit and did not take into account all of the federally provided funds on deposit by the Council in the same bank. The dollar amounts cited are at risk and if collateralized would result in savings in the event of a bank failure. Although the Council needs to insure and collateralize all of its federal deposits above \$100,000 to cover deposits at their highest level, or \$914,624 in this instance, only CBDG funds totaling \$188,177<sup>3</sup> would be put to better use.

## Conclusion

The City did not require the Council to collateralize the CBDG funds that it had on deposit. This occurred because the City did not take into account all of the federally provided funds on deposit by the Council in the same bank and reviewed only CBDG accounts, which at year end were below the FDIC limit. A total of \$188,177 in CBDG funds was not adequately collateralized and thereby protected against loss.

## Recommendations

We recommend that the director of the Office of Community Planning and Development in Boston require the City to

- 3A. Obtain and provide evidence that all federal funds in excess of FDIC limits for the Council are fully collateralized and thereby put \$188,177 in CBDG funds to better use by requiring and ensuring that these funds are adequately protected.
- 3B. Ensure that the Council redistributes the funds to other banks to bring deposits within FDIC limits if it is unable to obtain acceptable collateralization from the current financial institution.
- 3C. Ensure that the City develops a system to monitor deposits of all federal funds, including HUD-provided funds, to ensure that amounts in excess of FDIC limits are fully and properly collateralized.

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<sup>3</sup> The total for the two CBDG accounts was \$209,177 (\$110,990 plus \$98,187) as of January 31, 2006. This amount represents 21 percent (\$209,177 divided by \$1,014,624) of the total of \$1,014,624 for all accounts. The amount of CBDG funds covered by the \$100,000 in FDIC insurance coverage is \$21,000 (\$100,000 times 21 percent), and the amount of CBDG funds unprotected against loss is \$188,177 (\$209,177 minus \$21,000).

## RESULTS OF AUDIT

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### Finding 4: The City Did Not Ensure That Its Subrecipient Established Procedures to Prevent Potential Conflicts of Interest

The City did not ensure that its subrecipient, the New Bedford Economic Development Council (Council), did not issue loans that involved conflicts of interest. This deficiency occurred because the City believed that certain loans were outside of its review process and was unaware of any subrecipient loans that involved conflicts of interest. As a result, the subrecipient approved two loans totaling \$250,000 that created apparent conflicts of interest.

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#### **A Loan Was Issued to a Corporation Owned by a Board Member**

Under the subrecipient agreements, the Council is authorized to make loans including loans funded from Economic Development Administration (EDA) funds. The Council's loan program is subject to all CDBG regulations, including those pertaining to conflicts of interest, and prohibits the use of funds when conflicts of interest arise. The Council's staff processes all loans, including those not reported to the City.

The first conflict of interest noted occurred on June 24, 2004, when the Council provided a \$100,000 loan to a corporation that was owned by a Council member. There was no documented evidence of full disclosure before issuance of this EDA-funded loan, and the loan was not required to be reported to the City because it did not create jobs for low-to-moderate-income persons. The director of the City's Office of Housing and Community Development stated that the loan was not required to be reported to the City because it was outside of the City's review process and the City had no jurisdiction over the review or approval of the loan. Although these EDA funds do not pass through the City, the City does bear certain responsibilities with regard to all loans approved by the Council since the Council is funded under subrecipient agreements administered by the City. Also, since the City provides substantial funding towards the Council's loan program, it should ensure that the Council establishes adequate policies and procedures addressing conflict of interest issues. Although the loan was not reported to the City and the City may not have been aware of the loan, issuing loans to board members is not a prudent business practice because it could create apparent conflicts of interest and could lead to a pattern of conflicts in the future.



## **The Council's Chairman Benefited Directly from the Loan**

The second conflict of interest occurred on December 4, 2006, when the Council provided a loan that involved the Council's chairman. The \$150,000 loan was funded by \$110,000 in CDBG funds and \$40,000 in EDA funds. The loan was granted to provide working capital for the expansion of a company, and although the loan did not fund the expansion or construction, the construction work was completed by a firm owned by the Council's chairman. Therefore, the chairman directly benefited from the loan, and the use of CDBG funds to provide a loan was improper because a conflict of interest was created. In addition, the details regarding the chairman's personal involvement with the company receiving the loan were not disclosed to either the City or the Council before the loan was issued.

Although the chairman's personal involvement was not officially and fully disclosed to the City, loan documentation (facility report) submitted to the City indicated that the chairman's construction firm was involved in the expansion work. The City was familiar with this construction firm and its owner because the firm had been awarded contracts through procurements initiated by other subrecipients of the City (see finding 3).

## **Conclusion**

The Council approved two loans totaling \$250,000 that created apparent conflicts of interest. The practice of issuing loans to Council members or issuing loans that directly benefit Council members is not an efficient and effective use of federal funds and can lead to a pattern of conflicts in the future. These improprieties occurred because the City believed that certain loans were outside of its review process and were unaware that the loans involved conflicts of interest. The City recognizes that the Council must have a policy in place regarding conflicts of interest and full disclosure.

## **Recommendations**

We recommend that the director of the Office of Community Planning and Development in Boston require the City to

- 4A. Implement adequate controls to ensure that subrecipient loans do not involve conflicts of interest.

- 4B. Ensure that the Council establishes adequate policies addressing conflicts of interest including requirements for providing full disclosure.

## SCOPE AND METHODOLOGY

We performed an audit of CDBG and HOME programs administered by the City's Office of Housing and Community Development. Our fieldwork was completed at the City's Office of Housing and Community Development located at 608 Pleasant Street, New Bedford, Massachusetts, from September 2006 through January 2007. Our audit generally covered the period October 1, 2002, through September 30, 2006, and was expanded to cover other periods as needed. To accomplish our objectives, we

- Reviewed the *Code of Federal Regulations*, Office of Management and Budget circulars, HUD handbooks/guidebooks, and applicable HUD notices pertaining to the CDBG and HOME programs.
- Reviewed the City's policies and procedures and subrecipient agreements with the Council, the City's monitoring reports of the Council, and the results of prior independent public accountant and HUD reviews.
- Interviewed the City's mayor and HUD, City, and Council personnel.
- Evaluated the City's internal controls applicable to specific audit objectives.
- Determined whether CDBG and HOME program income earned by the City and subrecipients had been properly recorded and used in accordance with program requirements.
- Selected a non-representative sample of activities using the fiscal year 2004 Consolidated Annual Performance and Evaluation Report (CAPER) and traced data, including funds expended, status of activities, and reported accomplishments, from the CAPER to the City's records. The activities selected ranked second and third in dollar amount in the CAPER, and the activities for the Council ranked first in the amount of funding received, relative to a service or non-construction related activity in program year 2004. For this review, we identified a total of 35 activities (universe) excluding items categorized as "Infrastructure," "Public Facilities Improvements," and "Park Improvements."
- Evaluated the City's procurement practices through a review of three large construction contracts selected from the 2004 CAPER. The selection of the construction contracts was based on the three activities ranked the highest in funding received for a construction-related activity under the "Public Facilities Improvements" category shown on the CAPER. For this review, we identified a total of five activities (universe) under "Public Facilities Improvements" that were most similar to construction work and verified that the contracts were awarded fairly and resulted in full and open competition.
- Evaluated the adequacy of the City's administrative activities to ensure that administrative and planning costs did not exceed HUD funding limits and verified the reasonableness of salary allocations.
- Identified 18 loans reported by the Council that created and/or retained jobs for 2003, 2004, and 2005. We verified that loans met the public benefits standard of creating a minimum of one full-time job or retaining a minimum of one full-time job for each \$35,000 of investment and that at least 51 percent of the jobs were held by low- and moderate-income persons. We compared goals for the number of loans issued and new

jobs to be created under the subrecipient agreements to the results recorded by the City in its economic development monitoring reports.

- Reviewed the loan files for each of the 18 businesses that created/retained a job and verified that each file contained the following as required by the subrecipient agreements: (1) memorandum of agreement (showing the number of low- and moderate-income jobs to be created and retained by company), (2) employee income certification forms, (3) quarterly labor status report, (4) facility report (includes borrower analysis and financial analysis), and (5) final report whereby the Council reports that the business has fulfilled its goal of job creation. We also reviewed documentation to show that for job retention, jobs would have been lost without CDBG assistance.
- Selected a non-representative sample of loans that were issued to micro-enterprise businesses for review. From the universe of 11 loans, one loan was selected in each of the years (2003, 2004, and 2005) by largest dollar amount for a total of three loans to review.
- Selected a non-representative sample of five businesses for site visits from a universe containing 10 businesses that complied with or fulfilled the HUD requirement for jobs created/retained. The selection included businesses that created jobs showing the longest span of time between loan dates and compliance dates and ensuring that each program year was represented in the selection.
- Performed the site visits to confirm the job creation information reported by the City. During the site visits, we verified through review of payroll records that jobs created/retained actually existed and reviewed (1) payroll and employee records for businesses that retained jobs to ensure that income and family size were correct as reported on the employee certification forms; (2) the records of all employees who were hired and retained as well as those who had departed within the time the business received the loan through the compliance date; and (3) employee listings containing the names, addresses, start dates, and end dates of these employees.
- Grouped individual accounts together by bank for all banks used by the Council (subrecipient), reviewed ending balances for all accounts in the same bank for the 12 months of fiscal year 2005 (beginning with July 2005 and ending June 2006), computed totals for all accounts by month to identify the month with the highest balance for the 12-month period ending June 30, 2006, and computed the uninsured funds in the aggregate that exceeded FDIC limits.
- Obtained a listing of all loans issued by the Council for \$100,000 or more, covering the period from July 1, 2002, to June 30, 2006, and compared the names of individuals and/or principals of companies receiving the respective loans to names of Council board members, City Council members and all City employees to identify any potential conflicts of interest. For loans with apparent conflict of interest issues, we assured that adequate procedures were in place for proper underwriting of loans.
- Established that the City properly entered information on jobs created into the Integrated Disbursement and Information System.

We performed our review in accordance with generally accepted government auditing standards.

# INTERNAL CONTROLS

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Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

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## Relevant Internal Controls

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

- Controls to ensure that the grantee adequately monitors subrecipient management functions,
- Controls over the safeguarding of HUD funds,
- Controls over administrative costs,
- Controls over the tracking of program objectives,
- Controls to ensure that the grantee adequately monitors subrecipient reporting requirements,
- Controls over procurement and contracting, and
- Controls to prevent conflicts of interest.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

## Significant Weaknesses

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

- The City did not have adequate controls to ensure that its subrecipient issued the required number of loans and created the appropriate number of jobs.
- The City did not have adequate controls to ensure that its subrecipient completed all of the quarterly reporting requirements for job creation and retention.
- The City did not ensure that HUD funds maintained in subrecipient bank accounts were adequately protected against loss in case of a bank failure.
- The City did not adequately monitor its subrecipients' procurement and contracting processes.
- The City failed to properly monitor subrecipient loans for potential conflicts of interest.

## APPENDIXES

### Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Unreasonable or unnecessary 3/	Funds to be put to better use 4/
1C		\$750,000		
2A				\$285,000
3A				\$188,177
<b>Totals</b>		<b>\$750,000</b>		<b>\$473,177</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 polices 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 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/ Unreasonable/unnecessary costs are those costs not generally recognized as ordinary, prudent, relevant, and/or necessary within established practices. Unreasonable costs exceed the costs that would be incurred by a prudent person in conducting a competitive business.

4/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. This includes reductions in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings which are specifically identified. In Recommendation 2A, the \$285,000 represents the current year funds that would be used more efficiently if the specific program requirements in past and current agreements are met. In Recommendation 3A, the \$188,177 in HUD funds are at risk in the event of a bank failure; collateralizing these funds will protect them from this potential loss.


## Appendix B

# AUDITEE COMMENTS AND OIG'S EVALUATION

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### Ref to OIG Evaluation

### Auditee Comments

	<p><i>City of New Bedford</i> OFFICE OF HOUSING &amp; COMMUNITY DEVELOPMENT 608 Pleasant Street, New Bedford, Massachusetts 02740 Tel: (508) 979-1581 Fax: (508) 979-1575</p>	<p>HUD-01G OFFICE OF AUDIT BOSTON, MASSACHUSETTS 2006 APR -4 PM 2:41</p>
<p><b>PATRICK J. SULLIVAN</b> Director</p>		
<p>April 3, 2007</p>		
<p>Mr. John Dvorack Regional Inspector General for Audit, IAGA U.S. Department of Housing and Urban Development Office of Inspector General for Audit, Region I Thomas P. O'Neil Federal building 10 Causeway Street, Room 370 Boston, MA 02222-1092</p>		
<p>Dear Mr. Dvorack:</p>		
<p>I am writing in response to the audit of the City of New Bedford's Community Development Block Grant program (CDBG) and Home Investment Partnership Program (HOME) conducted by the Office of Inspector General HUD during the past several months further described in the Draft Audit Report presented to the City on March 21, 2007.</p>		
<p>The City welcomes the comprehensive review of these housing and community development programs and appreciates the opportunity to review and comment on the recommendations and findings further detailed in the Report.</p>		
<p>The City has taken the opportunity to examine in close detail the Audit Report's Findings and Concerns and have prepared a response with supportive documentation.</p>		
<p>In review of the Draft Audit Report dated March 21, 2007, I am appreciative of the comments, and recommendations for improvements cited by Inspector General staff. I fully agree with the Inspector General's opinion that the City of New Bedford is successfully implementing and carrying out eligible activities in accordance with HUD requirements, with the noted exception of four findings. Our response to these findings identifies a corrective action plan to remedy these findings and also identifies statements in the Audit Report that, in the City's opinion, are not consistent with the facts as presented in the report.</p>		
<p>The City continues to work under the stellar leadership and oversight of the HUD Region I Field Office and is continuously recognized by that office as administering federal entitlement programs in accordance with all applicable guidelines and regulations. I want to again thank you and your staff that conducted the monitoring visit and exit conference.</p>		



# AUDITEE COMMENTS AND OIG'S EVALUATION

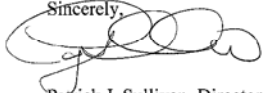
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Ref to OIG Evaluation

Auditee Comments

I look forward to working with you and your staff to provide any further information or clarification of our response as may be required.

Sincerely,



Patrick J. Sullivan, Director

cc:  
Honorable Mayor Scott W. Lang  
Robert Paquin, HUD CPD Director

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

CITY OF NEW BEDFORD RESPONSE TO THE  
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
OFFICE OF INSPECTOR GENERAL FOR AUDIT – DISCUSSION DRAFT AUDIT  
REPORT DATED MARCH 21, 2007

RESPONSE SUBMITTED BY: PATRICK J. SULLIVAN, DIRECTOR  
OFFICE OF HOUSING AND COMMUNITY  
DEVELOPMENT

RESPONSE DATE: APRIL 3, 2007

The following is the City of New Bedford's response to those Findings and Concerns raised in the Inspector General Draft Audit Report Monitoring Report. The City's response addresses each finding and concern in the order presented in the Audit Report. The City also addresses information contained in the Report that, in the opinion of the City, is not factually correct and/or requires correction. We have supplied relevant material and noted where the City has already taken corrective action.

### GENERAL COMMENTS

OIG Comment #1:

Page 7 first paragraph: "...The cost estimate of \$802,616 submitted by the sole bidder's architect pertained to the overall restoration and renovation of the subrecipient's operation and was based on a preliminary scope of work".

City's Response:

- The term sole bidder's architect should be corrected it is completely incorrect. The preliminary cost estimate was not submitted by the sole bidder. The cost estimate was submitted by the owner's architect, an independent third party architect hired by the owner. This should be corrected in the second sentence and again in the fourth sentence on page 7. That statement incorrectly states that the bidder hired the architect and had a cost estimate prepared by the bidder's architect. The City requests that this language be corrected.
- The report also states a project cost estimate of \$802,616. This amount represented the entire project costs that were projected to be completed in five years upon available funding acquired by the subrecipient. The City was not providing funding for the five year restoration plan. The City only committed \$250,000 in CDBG funds for the emergency repairs necessary to stabilize the building as outlined in the first phase cost estimate that totaled \$365,272, including alternates. The architect submitted a one year urgent need detailed cost estimate in the amount of \$365,272. The architect also included a five year preservation plan that detailed the preliminary construction costs over a five year period. The City requests that the cost estimate amount be corrected to reflect the work that was going to be paid with CDBG funding only.

Comment 1

Comment 2

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 3

OIG Comment #2:

Page 8 first paragraph: "... the cost estimate included additional costs associated with the reconstruction of the roof balustrade that were not included in the base bid.

City's Response:

This statement is incorrect. In review of the base bid and plans and specifications, the construction of the roof balustrade is clearly identified in Section 06300 "Architectural fiberglass reinforced polyester and aluminum balustrade" of the bid document. This scope was included in the contractor's bid price. This City requests that this statement be corrected.

Comment 4

OIG Comment #3:

Page 8 – first paragraph last sentence: "The subrecipient's decision to advertise the procurement in only the local newspaper may have limited the number of responsive bids".

City's Response:

The bid was advertised in accordance with City of New Bedford and HUD guidelines and requirements. The architect did in fact solicit proposals from qualified contractors by providing a copy of the invitation for bid to eligible bidders by mail. This was evidenced by the geographic representation by the eight contractors that picked up bid documents: 1) Warwick, RI, 2) Providence, RI, 3) Cranston, I, 4) Providence, RI, 5) Newton, MA, 6) Fall River, MA, 7) E. Providence, RI, and 8) Warren, RI.

Comment 5

In addition, the second subrecipient not only advertised the project in the local newspaper, the owner and the architect contacted several contractors to encourage their response to the advertisement for bids. In order to attract a wider geographic representation, the project was also listed in the Massachusetts Central Register, a statewide register that is reviewed by a substantial number of contractors. This helped to ensure that statewide contractors could review the invitation for bids.

Comment 6

OIG Comment #4

Page 9 – Under the Section entitled – "Subrecipients failed to perform Cost Analysis: The OIG Report states that both subrecipients failed to perform a cost analysis before awarding the contracts to sole bidders, and the cost estimate received by the second subrecipient appeared adequate."

City's Response:

The city is requesting that the statement be corrected to note that the second subrecipient did follow proper procedures in developing a cost estimate for construction of a two-level building as noted earlier in the Report.

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 7

### **FINDING #1**

The Inspector General Audit states that the City did not follow proper procedures with regard to the procurement of two construction projects. The City is hereby presenting information that states to the best of its ability and in the best interest of federal funding, the City did in fact take proper safeguards and assurances that the CDBG funding was in fact procured in accordance with HUD standards and was awarded to a contractor that presented a qualified bid that was well below the cost estimate.

### **FACTS -**

The architect prepared an itemized cost estimate for the proposed renovations to the building. The cost estimate included a detailed one year itemization of the most urgent repairs need to stabilize the building. The architect also completed a five year plan for future renovations to the building as part of an overall building restoration project. The City was only funding those repairs that were necessary to stabilize the building, as identified in the first year plan. The total cost estimate prepared by the architect for the first year renovations was \$365,272. The architect also provided the non-profit with a cost estimate for the five year restoration plan that totaled \$802,616.

Comment 8

The architect prepared the bid document with a base bid itemization that included work to the roof, gutters, chimney work and reconstruction, related painting, downspouts, drainage and front porch repairs. The aforementioned base bid items were all clearly itemized in the construction cost estimate. The architect also included, in the bid documents, three add alternates that were further detailed in the plans. These included Alternate One, masonry pointing, Alternate Two, the fiberglass parapet, and Alternate Three, lighting protection. The architect had also prepared detailed cost estimates for all of the "Add" alternate items.

Comment 9

The architect publicly advertised the project in accordance with HUD requirements. The architect also actively solicited interest from potential bidders by providing a copy of the invitation for bid. The bid solicitation resulted in a total of eight contractors place bid deposits for the project.

Comment 10

At the end of the bid period only one contractor submitted a bid proposal. The architect contacted several of the bidders in an attempt to determine why they had not submitted a proposal. The contractors that were contacted indicated that the project was relatively small in size, required the payment of prevailing wage rates and they felt that they did not have the required historic qualifications specified in the bid documents. It is important to note that the building that was renovated is a 180 year old federal style brick mansion listed on the National Register of Historic places as a contributing building to the County Street National Register Historic District. The bidding contractors were required to have specific experience working on historic properties over 100 years old in the last five years and have experience in the rehabilitation of older buildings in accordance with the Secretary of Interior Standards for Rehabilitation. This may have limited the number of respondents to the bid.

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 11

The architect presented the sole bid proposal to the City and the non-profit. The architect reviewed the bid and stated that the bid submitted was well within the cost estimate, and the architect noted that the contractor was preeminent in the historic restoration field and recommended to the non-profit that it was a fair bid. The architect reported that the base bid, which included the roof, gutters, chimney work and reconstruction, related painting, downspouts and drainage, and front porch work totaled \$339,525 compared to the estimate of \$316,036. Alternate One, the balance of the masonry pointing was \$55,000 versus the estimate of \$54,960, and Alternate Two, the fiberglass parapet totaled \$55,900 versus the estimate of \$93,600.

Based on the results of the bid coming in below the cost estimate and the experience of the contractor working on previous historic preservation renovation projects, the non-profit board of directors approved the acceptance of the contractor bid and secured the additional funding to cover constructions costs in excess of the City's commitment of \$250,000.

Comment 12

The second subrecipient not only advertised the project in the local newspaper, the owner and the architect contacted several contractors to encourage their response to the advertisement for bids. In order to attract a wider geographic representation, the project was also listed in the Massachusetts Central Register, a statewide register that is review by a substantial number of contractors. This helped to ensure that statewide contractors could review the invitation for bids.

### CITY'S RESPONSE TO FINDING #1:

It is the opinion of the City that the project was procured in accordance with federal requirements, advertised in local newspapers which resulted in the solicitation of eight contractors placing bid deposits to review the invitation for bids. While, the City would have liked to have additional bidders to maximize the competition, the sole bidder's proposal was well within the cost estimate. The architect, the non-profit and the City all agreed that the sole bidder's proposal was well within industry standards in terms of pricing and the contractor was more than qualified to carry out eligible historic preservation work. The project was completed on time, within budget and without any change orders. The project also received several awards for historic preservation.

Comment 13

In review of the cost estimate prepared by the architect, the Inspector General found that, while the cost estimate details the scope of work, the format is confusing and includes other detailed costs estimates. The cost estimate should be separated and reflect costs only associated with the scope of work in the bid document. The City agrees with this statement and is requesting the architect to prepare a cost estimate in the aforementioned format.

Regarding the second subrecipient construction project, the Report states that the second subrecipient did follow proper procedures in developing a cost estimate. The report also

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

states that the architect's estimate submitted by the sole bidder conformed to the contract and bid quotation. The City agrees with this statement.

### RECCOMENDATIONS:

- 1A. The City will continue to ensure that subrecipients comply with HUD requirements regarding the procurement of contractors to ensure an adequate number of contractors respond.
- 1B. The City will continue to ensure that subrecipients maintain adequate support showing that cost analyses are performed.
- 1C. The City will request that the first subrecipient obtain an itemized cost estimate from the architect that details the specific costs associated with the scope of work identified in the base bid documents
- 1D. The City will provide technical assistance to ensure that subrecipients follow procurement regulations.

### FINDING #2

The City agrees that the Council had difficulty in achieving the goals and objectives outlined in the subrecipient agreements during the three year period in question. The City continues to provide technical assistance to the Council and carefully monitors the economic development activities undertaken by the Council in order to ensure compliance with HUD requirements. The City has previously provided a reporting mechanism to the Council that carefully tracks the number of jobs created and/or retained and the number of low and moderate income jobs created or retained.

It is important to note that during the three year period, NBEDC did comply with all HUD reporting requirements regarding the public benefit standards. NBEDC did provide loans to eligible businesses and did create and or retain jobs of which 51% of such jobs were held by low and moderate income persons in accordance with HUD requirements.

In reviewing the Report, there is little mention of the job retention efforts undertaken by the Council during the three year period. The CDBG requirements cited under regulations CFR 570.203(b) "Special Economic Development Activities" state that eligible activities include the creation and or retention of jobs, 51% of such jobs created or retained must be held by low and moderate income persons. The City's Subrecipient Agreement with the Council, Inc. states "The Council shall be responsible herein for the administration, origination, processing, monitoring, reporting and portfolio management of loan programs that create and/or retain jobs for low to moderate income persons. Community Development Block Grant funding pursuant to these activities are authorized in accordance with Community Development Block grant regulations as follows: Special

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 14

Economic Development Activities – 24CFR570.203(b), Micro-Enterprise Assistance – 24CFR570.201(o).”

The City has always viewed that jobs that are either created and/or retained comply with the goals and objectives of the City’s Subrecipient Agreement and HUD regulations. The City of New Bedford’s economic development plan clearly articulates the need to provide assistance to existing businesses in order to “retain” current jobs.

During the three year period in question NBEDC provided a total of 30 loans, compared to the 36 loans required by the subrecipient agreement. During that same period, the Council created or retained a total of 66 jobs, compared to an overall goal of 60 jobs as stated in the subrecipient agreement. While, the Council should have had little difficulty in achieving these certainly attainable goals, the Council did achieve a level of compliance and success with the City’s goals and objectives by providing a total of 30 loans and actually exceeding the requirements by creating or retaining a total of 66 jobs.

The Council does continue to demonstrate a capacity to carryout eligible economic development activities. The Council is especially proficient in loan underwriting and lending. As a result of such high quality standards, less than 4% of all loans in the loan portfolio are delinquent.

### CITY’S RESPONSE TO FINDING #2:

Notwithstanding the above, the City will ensure that the Council achieves its goals and objectives outlined in the subrecipient agreement and consider imposing sanctions should the Council fail to fulfill its obligations without sufficient evidence to the contrary. The City will continue to work with the Council to ensure that it maximizes its outreach efforts to market its loan programs. Finally, the City will improve its control structure to ensure that the Council properly submits its quarterly labor status reports.

### RECCOMENDATIONS:

- 2A. The City will ensure that the Council will fulfill the requirements of its obligations to create jobs in accordance with subrecipient agreements.
- 2B. The City will ensure that the Council will meet its goals and objectives outlined in the subrecipient agreement and consider imposing sanctions should the Council fail to fulfill its obligations without sufficient evidence to the contrary.
- 2C. The City will ensure that the Council continues its outreach efforts to market its loan programs and to attract new businesses with the purpose of creating new jobs.
- 2D. The City will work with the Council to ensure the proper reporting of jobs created or retained.

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

### FINDING #3

The City did not take into account all of the federally provided funds on deposit by the Council in the same bank and reviewed only CDBG accounts, which at year end were below the FDIC limit.

### CITY'S RESPONSE TO FINDING #3:

The City agrees with the Inspector General Report's findings in finding #3 and the City will implement the following recommendations:

### RECCOMENDATIONS:

- 3A. The City has already implemented a plan with the Council to work with the financial institution to ensure that all federal funds in excess of FDIC limits are fully collateralized.
- 3B. The Council has assured the City that the current financial institution is in the process of collateralizing all federal funds.
- 3C. The City will implement a system to ensure that amounts in excess of FDIC limits are fully and properly collateralized.

### FINDING #4

The City agrees that the Council did in fact execute poor judgment in providing a loan, in 2003, to a member of the Board of Directors without full disclosure and review for any potential conflict of interest. The City also agrees that a full review and disclosure should have occurred when the Council provided a loan to a business that in turned hired the construction company owned by the Council President to construct a building. The City essentially agrees that the Council should have instituted internal controls to ensure that any potential conflict of interest would be reviewed and addressed prior to the approval of any loans.

### FACTS-

The City would like to note that in the first instance, the Council utilized a loan from a non-CDBG funding source and never presented the loan to the City for review and approval. The loan was never reported to the City in any documentation presented by the Council and the City had no way of knowing that this loan was provided to a member of the Council Board of Directors. Technically, the City had no jurisdiction over this loan because it was funded through a program that does not require City review or approval. The City provides approximately 45% of the Councils' total operating budget and only reviews those activities that are carried out in accordance with CDBG regulations.

Comment 15



# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 16

The second instance of a potential conflict of interest did involve a direct CDBG loan. The loan was presented to the City for approval. The loan facility report presented to the City described the loan, in the amount of \$110,000, as a working capital loan to expand an existing business. The City does not allow the Council to provide any CDBG loans for direct construction purposes. Therefore, all Council loans are limited to working capital activities. The Council provided the CDBG loan to the business, the business, in turn, applied for and received a second loan from a private bank in the amount of \$1.4 million for a plant expansion that included construction. The business hired a construction company that was owned, in part, by the chairman of the Council. In this instance, it was virtually impossible, for the City to determine that there was a potential conflict. The Council did not include any detailed information to the City regarding this potential conflict.

### CITY'S RESPONSE TO FINDING #4:

In order to ensure that the City will not be subjected to any potential conflicts of interest undertaken by the Council, the Council has volunteered to implement a comprehensive conflict of interest policy that must be executed by each Council member and Officer. The new conflict of interest policy ensures that a procedure will exist to independently review any potential conflict of interest prior to any action taken by the Council. The Council presented the new conflict of interest policy and conflict of interest procedures to the board of directors and they were accepted and incorporated into revised by-laws of the Council.

Comment 17

The Council has also reported to the City that the first recipient of the potential conflict of interest has resigned from the board of directors and is in the process of paying back the loan.

The Council, at its annual meeting held on March 20,2007, elected a new Chairman of the board, a new Treasurer and changed the by-laws to reflect the new comprehensive conflict of interest policy and procedures. The City will also implement the following recommendations:

### RECOMMENDATIONS:

- 4A. The City will require the Council to implement a comprehensive conflict of interest policy that must be executed by each Council member and Officer. The new conflict of interest policy will ensure that a procedure will exist to independently review any potential conflict of interest prior to any action taken by the Council.
- 4B. The aforementioned conflict of interest policy will delineate all policies addressing conflicts of interest including requirements for providing full disclosure.

# AUDITEE COMMENTS AND OIG'S EVALUATION

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## Ref to OIG Evaluation

## Auditee Comments

Comment 18

CITY OF NEW BEDFORD RESPONSE TO THE  
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT  
OFFICE OF INSPECTOR GENERAL FOR AUDIT – DISCUSSION DRAFT AUDIT  
REPORT DATED MARCH 21, 2007

**LISTING OF ATTACHMENTS:**

1. Correspondence dated February 22, 2005 from Newport Collaborative Architects describing the Bid Results from the first subrecipient identified in Finding # 1.
2. Register of Bid Documents from Newport Collaborative Architects listing all bidders on the project identified in Finding #1.
3. Bid Tabulation Sheet for the project identified in Finding #1.
4. Qualification statement describing the requirements necessary for contractors to bid on the first project identified in Finding #1.
5. Correspondence dated February 18, 2005, from contractor describing reasons that contractor did not bid on the first project identified in Finding #1.
6. Bid Document section describing scope of work to Roof Balustrade.
7. Correspondence dated April 8, 2005 from second subrecipient describing bid process identified in Finding #1.
8. Correspondence dated February 4, 2005 describing bidding requirements to the architect and owner identified as second subrecipient in Finding #1.
9. Copy of public advertisement for second subrecipient identified in Finding #1.
10. Copy of detailed cost estimate for the first subrecipient project identified in Finding #1.
11. Copy of New Bedford Economic Development Council conflict of interest policy.
12. Copy of New Bedford Economic Development Council conflict of interest procedures.

## OIG Evaluation of Auditee Comments

- Comment 1** The wording in the report was changed to show that the owner's architect submitted the cost estimate.
- Comment 2** The report was changed to note that the City committed to providing \$250,000 in CDBG funding only for the first phase work. With regard to the cost estimate for the first phase, we could not specifically identify or verify the cost estimate for the first phase. It appeared that the cost estimate for the first phase may have been included in the overall estimate of \$802,616. The City's staff indicated that the first phase cost estimate was \$677,624, and the architect failed to provide us the requested information regarding the cost estimate for the first phase. After we completed our audit work, we were informed by the City Director that the cost estimate for the first phase, totaling \$365,272, was for emergency repair work necessary to stabilize the building. We believe that the architect should have prepared a separate cost estimate for the first phase work regardless of how the work was to be funded.
- Comment 3** The statement that the base bid did not contain the costs associated with the reconstruction of the roof balustrade is a correct statement. Both the architect's written bid assessment, dated February 22, 2005, and the bid form (attachment # 3) provided in the Auditee's response show that the construction of the roof balustrade was not included as part of the base bid, but was included as alternate work at an additional cost of \$88,900.
- Comment 4** The bid for the first subrecipient was not advertised in strict accordance with HUD guidelines and requirements. Although eight contractors were provided a copy of the invitation for bid, only one contractor actually submitted a bid. HUD regulations require that for sealed bidding to be feasible, two or more responsible parties must be willing and able to compete effectively. Also, soliciting proposals from specific contractors by providing a copy of the invitation for bid, by mail, was not necessarily, in our opinion, the optimal method for advertising this procurement. Since only one bid was received, it would have been prudent to re-advertise. If the additional advertising failed to provide more than one bid, the City should have obtained a waiver from HUD to allow the contract to be awarded noncompetitively. In the report we noted that the first subrecipient advertised in only the local newspaper, and because only one bid was received, we questioned that decision.
- Comment 5** During our audit, we noted that the procurement for the second subrecipient was advertised in a local newspaper and in the Massachusetts Central Register.
- Comment 6** Although the second subrecipient did follow proper procedures in developing a cost estimate, both subrecipients failed to perform a cost analysis after it was

determined that adequate competition was lacking. The report was modified to reflect the need for a cost analysis when competition is inadequate.

**Comment 7** See explanation under Comment 2

**Comment 8** See explanation under Comment 3

**Comment 9** See explanation under Comment 4

**Comment 10** In its response, the City suggests that there may have been a limited number of respondents to the bid because the work required experience working on historic properties and experience in the rehabilitation of older buildings. The State of Massachusetts has a considerable number of old and historic structures. We believe that there are a reasonable number of companies within the state (and within New England) that are qualified to work on historic structures.

**Comment 11** See explanation under comment 3.

**Comment 12** See explanation under comment 5

**Comment 13** We acknowledge that the City agrees with OIG that the format for the cost estimate was confusing and that a separate cost estimate should have been prepared for the first phase work.

**Comment 14** The City stated that the Council created or retained a total of 66 jobs, compared to an overall goal of 60 jobs as stated in the subrecipient agreement, and that the Council achieved this goal by issuing a total of 30 loans. We acknowledge that the Council may have met the national objectives by either creating or retaining jobs. However, the specific goals in its agreements with the City for the 3 year period (2003 to 2005) were to issue 36 loans and create 60 new jobs. These requirements were stipulated in the agreements and the Council failed to meet these specific goals when they issued only 30 loans and created only 39 new jobs. There were no specific requirements in the agreements with the City with regard to the actual number of jobs to be retained.

**Comment 15** Although the loan was funded directly from a non-CDBG source, the City does bear certain responsibilities with regard to all loans made by the Council, since administrative salaries of the Council are supported primarily with CDBG funds. In addition, the subrecipient agreement executed between the Council and the City prohibits the use of funds when conflicts of interest arise. The Council's loan program is under the umbrella of the subrecipient agreements, and therefore, they are generally subject to all CDBG regulations, including those pertaining to conflicts of interest. Since the Office of Housing and Community Development is the only City department that the Council reports to, this Office is the logical entity to provide oversight and direction concerning these matters.

- Comment 16** In the second instance of conflict of interest, the City had the ability to determine that there was a potential conflict. As stated in our report, the facility report submitted by the Council to the City revealed that the board Chairman's construction company was involved in the expansion of an existing business. The City is familiar with this construction company, and its owner, because this company had been awarded contracts through procurements initiated by other subrecipients of the City.
- Comment 17** We acknowledge that the Council has made significant changes to address the conflict of interest issue. These include implementing a conflict of interest policy and replacing the board Chairman.
- Comment 18** The documents listed as attachments are not included in this Appendix as part of the auditee's response, due to their size. Many of the documents had previously been obtained during the audit and were already included in the work papers. The remaining attached documents have subsequently been placed into the work papers. These documents are available upon request.

## Appendix C

### LOANS ISSUED THAT CREATED AND RETAINED JOBS FOR PROGRAM YEARS 2003 TO 2005

2003

Number	Business	Program	Jobs created	Jobs retained
1	First café	Mass. Dev <sup>4</sup> .	3	0
2	Restaurant & tavern	EDA <sup>5</sup>	2	0
3	Grounds management	CELF <sup>6</sup>	1	0
4	Pizza restaurant	CELF-M <sup>7</sup>	0	0
5	Storage and truck rental	EDA	0	3
6	First real estate entity	EDA	5	0
7	Second real estate entity	Mass Dev.	4	0
8	Carpet service	CELF-M	0	0
9	Seafood restaurant	Mass. Dev.	1	0
10	Candy store	CELF-M	0	0
Totals			16	3

2004

Number	Business	Program	Jobs created	Jobs retained
1	T-shirt store	CELF-M	0	0
2	Convenience store	CELF-M	0	0
3	Sand & gravel (first loan)	CELF-M	0	0
4	Fish & chips	CELF	0	2
5	Freight company	EDA	2	0
6	Leather company	EDA	0	26
7	Dry cleaners	CELF-M	0	0
8	Carpet rental service	CELF	3	0
9	Painting & powerwashing	CELF-M	0	0
Totals			5	28

<sup>4</sup> Massachusetts Development Loan

<sup>5</sup> Economic Development Administration Loan

<sup>6</sup> Community Economic Loan Fund

<sup>7</sup> Micro-Enterprise Loan Fund

## Appendix C

2005

Number	Business	Program	Jobs created	Jobs retained
1	Restaurant	CELF	5	0
2	Taxi service	CELF-M	0	0
3	Hot dog restaurant	CELF-M	0	0
4	Painting contractor	CELF-M	0	0
5	Second café	CELF	1	0
6	Sand & gravel (second loan)	EDA	2	0
7	Boat propeller sales/repairs	EDA	1	0
8	First fishing enterprise	EDA	3	0
9	Car wash	CELF	3	0
10	Child day care center	CELF Area Benefit Loan	0	0
11	Second fishing enterprise	EDA	3	0
Totals			18	0

## Appendix D

### QUARTERLY LABOR STATUS REPORTS

Business	Jobs created or retained	Loan date	Final report date	Problems noted
Restaurant/tavern	2 created	May 10, 2004	Apr. 11, 2005	Reports not submitted in a timely manner and reports missing
First café	3 created	June 14, 2004	Sept. 25, 2006	Reports not submitted in a timely manner and reports missing
Storage/truck rental	3 retained	Dec. 18, 2003	Jan. 22, 2004	Reports not required (see note 8)
Seafood restaurant	1 created	Sept. 29, 2003	Jan. 22, 2004	No problems noted
First real estate entity	5 created	Nov. 12, 2003	Jan. 22, 2004	One report required and submitted but not dated
Grounds management	1 created	Apr. 8, 2004	July 12, 2006	Reports not submitted in a timely manner and reports missing
Second real estate entity	4 created	Nov. 10, 2003	Jan. 22, 2004	No problems noted
Leather company	26 retained	Feb. 1, 2005	Feb. 14, 2005	Reports not required (see note 7)
Fish & chips	2 retained	Mar. 10, 2005	Apr. 1, 2005	Reports not required (see note 7)
Freight company	2 created	Mar. 1, 2005	Mar. 24, 2005	Reports not required (see note 7)
Carpet rental service	3 created	Dec. 6, 2004	Not applicable (see note 9)	No reports submitted
Restaurant	5 created	Jan. 12, 2006	Sept. 20, 2006	Reports not submitted in a timely manner and reports missing
First fishing enterprise	3 created	Apr. 13, 2006	Not applicable (see note 8)	No reports submitted
Boat propeller sales/repairs	1 created	Mar. 22, 2006	Not applicable (see note 8)	No reports submitted
Sand & gravel (2 <sup>nd</sup> loan)	2 created	Apr. 6, 2006	Not applicable (see note 8)	No reports submitted
Second café	1 created	Apr. 3, 2006	Not applicable (see note 8)	No reports submitted
Car wash	3 created	May 31, 2006	Not applicable (see note 8)	No reports submitted
Second fishing enterprise	3 created	Feb. 1, 2006	Mar. 28, 2006	Reports not required (see note 7)

<sup>8</sup> Since the time between the date of loan issuance and the final report date is less than two months, submission of quarterly labor status reports would not be deemed necessary. The final report date is the date job creation/retention goals are fulfilled, at which time businesses are no longer required to submit the quarterly labor status reports.

<sup>9</sup> Businesses have two years from the date of the loan to meet goals for job creation/retention, at which time a final report is executed.



## Appendix E

### BALANCES IN TEN BANK ACCOUNTS AS OF JANUARY 31, 2006

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<b>Account number</b>	<b>Amount</b>	<b>Federal account</b>
xxxxx684	\$ 16,937	EDA <sup>10</sup>
xxxxx424	32,098	EDA
xxxxx700	164,261	EDA
xxxxx692	25,704	EDA
xxxxx416	298,774	EDA
xxxxx042	110,990	HUD
xxxxx069	98,187	HUD
xxxxx743	267,473	EDA
xxxxx192	100	EDA
xxxxx232	100	EDA
<b>Total dollar amount</b>	<b>\$1,014,624<sup>11</sup></b>	
<b>Less FDIC coverage</b>	<b>100,000</b>	
<b>Uninsured amount</b>	<b>\$ 914,624</b>	

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<sup>10</sup> U.S. Economic Development Administration funding

<sup>11</sup> Rounded to the nearest dollar amount

## Appendix F

### CRITERIA

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#### Regulations at 24 CFR [*Code of Federal Regulations*]

- 570.501(b) states that the recipient is responsible for ensuring that the CDBG funds are used in accordance with all program requirements. The use of designated public agencies, subrecipients, or contractors does not relieve the recipient of this responsibility. The recipient is also responsible for determining the adequacy of performance under subrecipient agreements and procurement contracts and for taking appropriate action when performance problems arise.
- 570.503(a) states, in part, that the recipient shall sign a written agreement with the subrecipient. CFR 570.503(b)(2) further states that the recipient shall specify in the agreement with the subrecipient the particular records the subrecipient must maintain and the particular reports the subrecipient must submit to assist the recipient in meeting its recordkeeping and reporting requirements.
- 85.20(b)(3) states that “effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes.”
- 570.502(b) requires that subrecipients, except subrecipients that are governmental entities, shall comply with the requirements and standards of Office of Management and Budget (OMB) Circular No. A-110, “Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations.” OMB Circular A-110, subpart C, section 21(b)(3), requires “effective control over and accountability for all funds, property and other assets. Recipients shall adequately safeguard all such assets and assure they are used solely for authorized purposes.”
- 85.36(b)(9) requires grantees and subgrantees to maintain records sufficient for the basis of contract price.
- 85.36(c)(1) requires all procurement transactions to be conducted in a manner providing full and open competition.
- 85.36(d)(2)(i)(B) requires that for sealed bidding to be feasible, two or more responsible bidders are willing and able to compete effectively and for the business.
- 85.36(d)(4) states that procurement by noncompetitive proposals may be used only when the award of a contract is infeasible under small purchase procedures, sealed bids, or competitive proposals and one of the following circumstances applies: (A) the item is available only from a single source; (B) the public exigency or emergency for the requirement will not permit a delay resulting from competitive solicitation; (C) the awarding agency authorizes noncompetitive proposals; or (D) after solicitation of a number of sources, competition is determined inadequate.
- 85.36(d)(4)(ii) for noncompetitive proposals further states that a cost analysis; i.e., verifying the proposed cost data, the projections of the data, and the evaluation of the specific elements of costs and profits, is required.

- 85.36(f)(1) requires that the subrecipient perform a cost or price analysis in connection with every procurement action, including modifications. The method and degree of analysis is dependent on the facts surrounding the particular procurement situation, but as a starting point, the City must make an independent estimate before receiving bids or proposals. A cost analysis will be necessary when adequate price competition is lacking.
- 570.611 states that no employee of the recipient, officer, or elected official or appointed official of the recipient or of any designated public agencies or of subrecipients that receive funds, who exercise or have exercised any functions or responsibilities with respect to CDBG activities or who are in a position to participate in a decision-making process or gain inside information with regard to such activities, may obtain a financial interest or benefit from a CDBG-assisted activity or have a financial interest in any contract, subcontract, or agreement with respect to a CDBG-assisted activity, either for themselves or those with whom they have a business or immediate family ties, during their tenure or for one year thereafter.

The subrecipient agreement executed by the Council and the City

- Part I, section I(E), states that the City will monitor the performance of the Council against goals and performance standards. Substandard performance, as determined by the City, will constitute noncompliance with this agreement. If action to correct such substandard performance is not taken by the Council within a reasonable period after being notified by the City, suspension or termination procedures will be initiated.
- Part II (Scope of Services), section II, states that the Council is required to carry out project activities consistent with program objectives. These program objectives include requiring the Council to provide a minimum of 12 loans to eligible companies and/or micro-enterprises and to create a minimum of 20 new jobs through such loans.
- Part II (Scope of Services), section IV, requires that, on a quarterly basis, the Council shall provide the City with reports detailing the monitoring of job creation and/or job retention initiatives for the administration of all applicable CDBG revolving loan funds and the monitoring of job retention initiatives within the administration of all applicable CDBG revolving fund activities. Part II, section IV(D), further requires the Council to complete and provide to the City a confidential quarterly labor status report for each loan every quarter (three months). This form shall be sent by the Council to all businesses receiving loan funds. This form will be used to monitor the compliance of loan activity with HUD regulations. This report shall contain the total number of employees of the borrower/debtor at the commencement of the loan, the total number of employees at the beginning of the reporting period, and the full-time/part-time equivalent jobs created and jobs retained during said quarter. The report shall also contain the nationality of the individuals filling the jobs as well as the signature of the debtor/employer.
- Section II(21) states that the construction procurement standards established by the City shall be imposed by the Office of Housing and Community Development. The federal contract provisions established by HUD and adopted by the City shall be included in all construction contracts funded in whole or in part by CDBG funding.
- Part I, section V(A), states that the subrecipient agrees to comply with the requirements of 24 CFR Part 570 (HUD CDBG regulations). The subrecipient also agrees to comply with all other applicable federal, state, and local laws, regulations, and policies governing the funds provided under this agreement.

- Part I, section VIII(D)(4), states that the subrecipient agrees to abide by the provisions of 24 CFR 570.611 with respect to conflicts of interest and covenants and that it presently has no financial interest and shall not acquire any financial interest, direct or indirect, which would conflict in any manner or degree with the performance of services required under this agreement. Further, no officer, member, or employee of the City and no members of its governing body and no other public official of the governing body of the locality or localities in which the project is situated or being carried out, who exercise any functions or responsibilities in the review or approval of the undertaking or carrying out of this project during their tenure in office or for one year thereafter, shall participate in any decision relating to this agreement which affects their personal interest or the interest of any corporation, partnership, or association in which they may be, directly or indirectly, interested or have any personal or pecuniary interest, direct or indirect, in this agreement.
- Part I, section VI(A)(2), states that subrecipients who are governmental and quasi-governmental agencies must comply with applicable sections of 24 CFR Part 85, “Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments.”

According to FDIC rules, the basic insurance amount is \$100,000 per depositor, per insured bank. FDIC insurance covers all types of deposits received at an insured bank, including deposits in checking accounts, interest-bearing negotiable order of withdrawals (NOW) accounts, savings accounts, money market deposit accounts, and time deposits such as certificates of deposit (CD). All accounts of a public unit in the same bank will be insured up to \$100,000 in the aggregate.

The U.S. Treasury Financial Manual, part 6, chapter 9000, describes federal agency requirements to secure public money on deposit at financial institutions. Section 9010 of part 6, chapter 9000, states “Agencies must ensure the security of public money. Public money includes, but is not limited to, revenue and funds of the United States and any funds the deposit of which is subject to the control or regulation of the United States or any of its officers, agents or employees.” According to 6-9040.20—Securing Deposits with Collateral, “When an agency deposits public money exceeding the recognized deposit insurance limit (generally \$100,000), the agency must request that the depository pledge eligible collateral to secure the uninsured amount. The depository must pledge collateral with a Federal Reserve Bank (FRB) or an authorized third-party custodian approved by the FRB. If a third-party custodian is used, the depository must notify the FRB by a trust receipt. The National Customer Service Area (NCSA) must ensure the depository pledges collateral according to the list of ‘Acceptable Collateral for Pledging to Federal Agencies’ under 31 CFR 202 and 380.”