



OFFICE *of*
INSPECTOR GENERAL
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UNITED STATES DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT

Office of Community Planning and Development, Community Development Block Grant Disaster Recovery Funds

State of North Carolina, Morrisville, NC | 2022-AT-1002

September 16, 2022

Date: September 16, 2022

To: Elizabeth S. Hendrix
Acting Deputy Assistant Secretary, Office of Deputy Assistant Secretary for Grant Programs, DG

From: *//signed//*
Kilah S. White
Assistant Inspector General for Audit, GA

Subject: The State of North Carolina Generally Had Capacity and Mostly Followed Disbursement Requirements, but Its Procurement Process Needs Improvement

Attached are the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the State of North Carolina, Office of Recovery and Resiliency's Community Development Block Grant Disaster Recovery funds.

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

The Inspector General Act, Title 5 United States Code, appendix 8M, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at <https://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call Nikita N. Irons, Audit Director, at (404) 331-3369.

Executive Summary

OFFICE OF COMMUNITY PLANNING AND DEVELOPMENT, COMMUNITY DEVELOPMENT BLOCK GRANT DISASTER RECOVERY FUNDS | 2022-AT-1002

What We Audited and Why

We audited the State of North Carolina's Community Development Block Grant Disaster Recovery (CDBG-DR) funds. We initiated this audit as part of our commitment to helping the U.S. Department of Housing and Urban Development (HUD) address its top management challenges and to support HUD's strategic objective to support effectiveness and accountability in long-term disaster recovery. Further, Congress has expressed strong interest in HUD's disaster programs.

Our audit objective was to determine whether the State had sufficient capacity to administer its CDBG-DR funds and followed disbursement and procurement requirements related to those funds.

What We Found

The State generally had capacity. It had staffing capacity, maintained an internal auditor position, and had policies in place for administering CDBG-DR funds. The State also mostly followed disbursement requirements. Of the 25 disbursements reviewed, only 3 (12 percent) were not adequately supported with required documentation. However, the State's procurement process needs improvement. The three procurements reviewed lacked or did not have adequate documentation to support (1) that cost reasonableness was properly assessed or (2) that it prepared independent cost estimates before the bidding process as required by Federal regulations and its own policy, respectively. These conditions occurred because the State did not follow its disbursement procedure and did not fully understand the procurement requirements. In addition, the State's procurement policy did not clearly address the procurement process for its staff to follow. As a result, the State could not provide reasonable assurance to HUD that more than \$2.5 million of \$5.4 million in CDBG-DR funds reviewed was spent properly.

What We Recommend

We recommend that the Deputy Assistant Secretary for Grant Programs require the State to (1) provide adequate documentation to support that more than \$2.5 million in CDBG-DR funds was spent for necessary and reasonable costs or repay the funds, (2) update its procurement policy, and (3) provide training to its staff to ensure that it understands and follows requirements to maintain adequate documentation to support program disbursements that are eligible and reasonable and procurement requirements, including completing independent cost estimates and cost analyses.

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Background and Objective

On October 8, 2016, Hurricane Matthew struck North Carolina with hurricane and tropical storm force winds, rain, and storm surge, causing the loss of life and extensive damage to homes, businesses, and infrastructure. Through the Disaster Relief Appropriations Acts of 2016 and 2017, Congress made funds available in Community Development Block Grant Disaster Recovery (CDBG-DR) grants for disaster relief, long-term recovery, restoration of infrastructure, and housing and economic revitalization. Specifically, under Public Laws 114-223, 114-254, and 115-31, the U.S. Department of Housing and Urban Development (HUD) appropriated more than \$236.5 million in CDBG-DR funding to the State, which was available for drawdown based on a grant agreement between the State and HUD, executed on August 15, 2017.¹ As of March 22, 2022, the State had more than \$91 million to draw down in CDBG-DR funds, which is shown in the table below.

Disaster Year	Total grant	Amount drawn as of 3/22/2022	Remaining amount as of 3/22/2022
2016	\$236,529,000	\$145,331,184	\$91,197,816

Beginning in August 2017, the State's Department of Commerce (Commerce) administered CDBG-DR funds. Specifically, Commerce entered into a programmatic agreement with the North Carolina Department of Public Safety, Division of Emergency Management (Emergency Management), on April 26, 2018, stating that Commerce would administer the grant while Emergency Management would implement the grant. However, in October 2018, the State's governor approved legislation that created a new entity, the North Carolina Office of Recovery and Resiliency (NCORR), within the State's Department of Public Safety, to administer CDBG-DR funds. NCORR began operations in January 2019 and began administering the CDBG-DR funds, except for processing drawdowns, which it took over when it was made the grantee of record by HUD. On July 1, 2019, HUD approved the State's request and recognized NCORR as the administering agency responsible for all CDBG-DR funds discussed above.² NCORR used the same CDBG-DR action plan³ that Commerce had developed.

Our audit objective was to determine whether the State had sufficient capacity to administer its CDBG-DR funds and followed disbursement and procurement requirements related to those funds.

¹ The grant agreement was amended once on March 15, 2018, to increase the initial funding of \$198,553,000 by \$37,976,000, bringing the total amount to \$236,529,000 in CDBG-DR funds.

² The change in grantee occurred after we started our review. Therefore, our review included disbursements and procurements processed by or under both Commerce and NCORR. However, our audit recommendations relate to NCORR as it was the responsible entity representing the State to HUD. Therefore, State and NCORR are used interchangeably in this report.

³ The CDBG-DR action plan described the State's analysis and plan to allocate available funding to a combination of housing, economic development, infrastructure, and services programs.

Results of Audit

FINDING: THE STATE OF NORTH CAROLINA GENERALLY HAD CAPACITY AND MOSTLY FOLLOWED DISBURSEMENT REQUIREMENTS, BUT ITS PROCUREMENT PROCESS NEEDS IMPROVEMENT

The State generally had sufficient capacity to administer its CDBG-DR funding and mostly followed requirements for disbursing CDBG-DR funds, but its procurement process needs improvement. The State demonstrated staffing capacity and maintained and updated policies for administering the CDBG-DR funds. Of the 25 disbursements reviewed, only 3 (12 percent) were not adequately supported with required documentation. In addition, the State did not follow its procurement requirements for the three procurements reviewed. Specifically, it lacked documentation or did not maintain adequate documentation to support (1) that the cost reasonableness of the contracts procured was properly assessed or (2) that it prepared independent cost estimates before the bidding process as required by Federal regulations⁴ and its own policy⁵ respectively. In addition, for one procurement, the State did not perform a timely review of the excluded parties list for determining contractor eligibility. These conditions occurred because the State did not follow its disbursement procedure and did not fully understand the procurement requirements and its procurement policy did not clearly address the procurement process. As a result, the State could not provide reasonable assurance to HUD that more than \$2.5 million in CDBG-DR funds was properly spent.

The State Generally Had Sufficient Capacity

The State generally had sufficient capacity for administering its CDBG-DR funds. Specifically, the State demonstrated capacity by filling staffing vacancies, maintaining an active internal auditor function, and maintaining and updating policies for administering CDBG-DR funds. At the time of our review, all 4 top leadership roles were occupied, and 3 of 20 senior staff positions were vacant; however, after we communicated the initial results of our review, the State filled all 3 senior staff positions. The staff's employment history included an average of 1.3 years' experience and demonstrated training received related to CDBG-DR. In addition, the State had contracted with four firms to assist in administering the CDBG-DR funds. Among these four contracted firms, the State had the support of contracted employees to assist in covering all aspects of the programs, to include construction, program management, and information technology.

In addition, as required,⁶ the State maintained an independent internal auditor position through an interagency agreement with the North Carolina Office of State Budget and Management. At the time of our review, the internal auditor position was maintained on a part-time basis. However, after we communicated the initial results of our review on January 14, 2020, two internal auditors were assigned specifically to review the disaster recovery funds. Further, on February 8, 2021, State officials stated that

⁴ 2 CFR (Code of Federal Regulations) 200.323(a), 2 CFR 200.318(i), and 2 CFR 200.404 (December 19, 2014).

⁵ Section IX of the State's procurement manual, dated March 2019, and "Cost and Price Requirements" section in the State's crosswalk, or "Federal and State Procurement Comparison Chart" for Hurricane Matthew disaster recovery grant.

⁶ A Federal Register (FR) notice, 81 FR 83254, section VI (A)(1)(b)(2)(b), required an internal auditor position, reporting independently to the chief elected or executive officer of the governing body of the administering entity.

the auditors had reviewed six allegations of fraud, waste, and abuse and had begun auditing the Manufactured Housing Unit Program in November 2020.⁷

The State Mostly Followed Requirements for Disbursing CDBG-DR Funds

To determine whether the State followed requirements for disbursing CDBG-DR funds, we selected and reviewed 25 expenditures totaling nearly \$5.5 million (27 percent) from a universe of 143 expenditures totaling more than \$20.5 million.⁸ We determined that the State followed its disbursement requirements to ensure that adequate support was obtained and maintained before processing, except for 3 of the 25 (12 percent) disbursements reviewed. All three expenditures were for monthly project management services, which was one of seven tasks⁹ under one contract to one vendor. This contract was procured by Emergency Management under Commerce's administration of CDBG-DR funds. Therefore, NCORR continued working with the vendor under the same contract once it took over administration of the CDBG-DR program.¹⁰ Of the three payments in question, two were issued by Commerce, and one was processed and paid by NCORR. While the contract for project and program services and management was awarded on a unit-price¹¹ basis, it stated that invoices must include an accurate description of the work for which the invoice was submitted, the invoice date, the period of time covered, the amount of fees due to the vendor, and the original signature of the vendor's project manager.¹² However, none of the three expenditures had adequate documentation to sufficiently document the allowability of the cost.

The requirement for having supporting documentation for the unit-price contract caused confusion because while timesheets or progress reports were not required due to the contract type,¹³ the vendor was required to sufficiently document performance or provide deliverables in accordance with 2 CFR 200.459(b)(8) (December 19, 2014).¹⁴ NCORR reached out to HUD for guidance regarding the appropriate supporting documentation needed for program management service under a unit priced contract. After receiving technical assistance from HUD, NCORR's finance chief issued a memorandum to the accounting team, stating that the contract did not include requirements regarding invoice

⁷ The Manufactured Housing Unit Program was one of several disaster recovery efforts funded by the CDBG-DR funds.

⁸ See the Scope and Methodology section of this report for details on our sample selection.

⁹ The seven tasks included in the contract for project and program services and management were as follows: (1) eligibility requirements, (2) duplication of benefits, (3) site inspections, (4) lead-based paint testing, (5) project-specific environmental review, (6) monthly project management, and (7) monthly case management. The three vouchers we reviewed included charges related only to task 6. Further, none of the remaining 22 (25 – 3) expenditures were of the same vendor but, rather, were payments issued to other vendors, subrecipients, or individual homeowners. Therefore, our review did not include charges related to any of the other six tasks for the vendor in question.

¹⁰ See footnote 2 and the Background and Objective section of this report for details.

¹¹ In accordance with 2 CFR 200.201(b)(1)(ii), payments to contracted vendors on a unit-price basis means payments for a defined unit(s) at a defined price(s), which are agreed upon in advance of contract execution and detailed as such in the contract.

¹² See appendix C for the contract requirements related to vendor invoicing.

¹³ Regulations at 2 CFR 200.201(b)(1) state that fixed amount awards can be used if the project scope is specific and if adequate cost, historical, or unit pricing data are available to establish a fixed amount award with assurance that the non-Federal entity will realize no increment above actual cost.

¹⁴ In accordance with 2 CFR 200.459(b)(8), the adequacy of the contractual agreement for the service (for example, description of the service, estimate of time required, rate of compensation, and termination provisions) is a relevant factor in determining the allowability of costs.

presentation. The memorandum provided details regarding invoice presentation and included a template¹⁵ to be used for the vendor's invoicing against the contract for monthly project management.¹⁶

Although NCORR's finance chief addressed invoice presentation for the contract type, the State did not follow the procedure when it issued payment, and the invoices lacked sufficient detail to describe the work performed. Specifically, the guidance provided to the accounting team included a summary report of program management-related effort, which served as a template for reviewing and approving invoices for program management services. The guidance stated that the description under the effort category should be sufficient to detail the work performed. However, the invoice documentation for the three disbursements was inconsistent and not adequate.

None of the three expenditures totaling more than \$2.5 million included adequate documentation to support the allowability of the cost. The support documentation did not include the template or all information in the template or have an accurate description of the work for which the invoice was submitted. The support documentation included with the three expenditures in question is as follows.

1. Invoice documentation for expenditure 1: Covered a period of 2 months (March and April 2019) and included a memorandum from the vendor with an overview of the activities completed since the beginning of the contract term (June 2018) instead of an accurate and specific description of the work completed for the 2 months invoiced.
2. Invoice documentation for expenditure 2: Covered a period of 8.5 months and included memorandums from the vendor with the statement of work from the contract and a schedule including the employees' names, the number of hours charged, and a column titled "effort category." However, the schedule did not provide the employees' position title, and the effort category did not include a description sufficient to detail the work completed. Instead, the effort category included a job description for the position title. For example, the schedule noted that the following work was completed in 4 hours: "Site Inspections, including but not limited to the direct supervision and management of Inspection staff, coordination with Environmental Review – staff and to provide quality assurance and quality control for Environmental Reports."
3. Invoice documentation for expenditure 3: Covered a period of 1 month and included the template provided in NCORR's finance chief's memorandum. However, the effort category did not include sufficient detail for work completed. For example, the effort category for the program administrator stated only, "...program management including but not limited to Program Administration and Coordination." Further, the template included position titles such as appeals specialist and environmental review specialist, which were not listed in the contract where the unit price was calculated.

The 2 CFR 200.403 (December 19, 2014) provides that costs must be adequately documented to be allowable under Federal awards. As detailed above, the State did not follow its own requirements under

¹⁵ The invoicing template required the following information: employee name, position title, week ending, project hours, description of effort, supervisor name, employee certification date, supervisor approval date, project manager's signature, invoice number, invoice date, and the person preparing the template.

¹⁶ All three of the payments were made after the issuance of the finance chief's memorandum, dated May 28, 2019.

the contract or the clarification memorandum issued by the finance chief for obtaining and maintaining adequate supporting documentation. As a result, we could not determine whether more than \$2.5 million in CDBG-DR expenditures was used in accordance with the requirements.

The State’s Procurement Process Needs Improvement

The State’s procurement process needs improvement. Specifically, the State did not follow procurement requirements for administering CDBG-DR for the contracts reviewed. We selected and reviewed three contracts, representing nearly 82 percent (\$68.6 million) of the universe in dollars from the eight contracts procured by the State totaling more than \$83.5 million. All three of the contracts reviewed lacked or did not have adequate documentation to support (1) that cost reasonableness was properly assessed or (2) that it prepared independent cost estimates before the bidding process as required by Federal regulations¹⁷ and its own policy¹⁸, respectively. Additionally, for one contract, the State did not perform a timely review of excluded parties¹⁹ in assessing the contractor’s eligibility. The procurement deficiencies noted in our review are summarized in the table below.

Type of contract	Contract date	Contract amount	Procurement deficiencies noted			
			Untimely cost estimation	Unsupported cost estimates	Inadequately supported cost analysis	Untimely determination of vendor eligibility
Project and program services and management	06/15/18	\$16,703,125		X		
Program management services	09/03/19	34,996,390	X			
Construction management services	05/09/19	16,876,604	X	X	X	X

¹⁷ See footnote 4.

¹⁸ See footnote 5.

¹⁹ The U.S. General Services Administration maintains a list of parties that are excluded from receiving Federal contracts, certain subcontracts, and certain types of Federal financial and nonfinancial assistance and benefits. Exclusions are also referred to as suspensions and debarments.

Cost Reasonableness Was Not Adequately Supported

To support the cost reasonableness of contracts, Federal regulations require (1) independent cost estimates before receiving bids or proposals and (2) a cost or price analysis in connection with every procurement action.²⁰

For the construction management services contract, the procurement file did not include adequate documentation of an independent cost estimate and a cost analysis for a contract price increase. The State did not complete a timely cost estimate before issuing the proposals request for this contract²¹ in accordance with its own policy.²² Although the cost estimate was completed before the proposals were received, the cost estimate was \$11.6 million less²³ than the average proposed cost in the received proposal documentation and, thus, insufficient to support the contract price. Independent cost estimates should be used to help adequately budget and to determine whether proposed pricing is reasonable before entering into a contract. Federal regulations²⁴ provide that a cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The State explained that it had underestimated the needed number of hours under the contract, resulting in its low cost estimate. However, this information was not in the procurement file to sufficiently document the resolution of the disparity between the cost estimate and the awarded amount and detail the history of the procurement.²⁵

The State provided a memorandum entitled “Cost Analysis,” which was not an analysis of proposals received but, instead, was the State’s cost estimate for the contract. The memorandum stated that to determine cost reasonableness, staffing rates should be analyzed on a per-hour basis as included in the issued request for proposal. Specifically, the memorandum summarized the proposal request requirements that the vendors’ proposals include a staffing plan composed of key and other construction management personnel, hourly rates associated with each position, total estimated hours per position per month, total estimated cost per position per month, and total estimated cost for all positions per

²⁰ 2 CFR 200.323(a) (December 19, 2014)

²¹ We noted a similar exception with the program management services contract in which the State did not complete a timely cost estimate before issuing the proposals request.

²² The Federal requirements at 2 CFR 200.323(a) (December 19, 2014), required completion of cost estimate before receiving bids or proposals, but the State had a stricter policy in this regard. Specifically, Section IX of the State’s procurement manual, dated March 2019, labeled “Total Process Overview” provides an overview of the procurement process in a table format, listing item 4 as “Conduct cost/price analysis” and item 7 as “Post the procurement opportunity on the state procurement website.” Further, in the “Cost and Price Requirements” section of the State’s “Federal and State Procurement Comparison Chart” for Hurricane Matthew disaster recovery grant, states that the State will include the following language in its Procurement Manual: “[the State] shall ensure that a cost or price analysis is conducted for all contracts costing \$250,000 or more prior to soliciting bids.” This excerpt did not include any limitations whether the procurement type was competitive or noncompetitive.

²³ The State estimated \$4,623,186 and awarded the contract for \$16,876,604, but the average proposal cost for six proposals received, including the winning contractor, totaled \$16,269,497. Therefore, its estimate was \$11.6 million less than the cost estimate in the received proposals (\$16,269,497 – \$4,623,186).

²⁴ 2 CFR 200.404 (December 19, 2014)

²⁵ The State’s procurement policy provided that it was equivalent to Federal regulations at 2 CFR 200.318 through 200.326 (December 19, 2014). According to 2 CFR 200.318(i) (December 19, 2014), a non-Federal entity must maintain records sufficient to detail the history of the procurement.

month. However, for the six proposals received, the State did not use staffing rates to determine cost reasonableness. Instead, scores were assigned to each vendor for the cost category²⁶ based on how the total cost for each proposal compared to the lowest cost proposal.

The State disagreed with our assessment and stated that it used the per-hour basis and provided additional documentation to show that the winning contractor's estimate was assessed and that it was lower than the State's estimate based on 173 monthly hours. Although the estimate was lower, there was a significant difference in the number of hours estimated by the State and the winning contractor. For example, the State estimated that the field inspector position would have three positions for a total of 519 hours per month based on its estimate of 173 hours per month per inspector (519 hours/173 hours per month). However, the winning contractor estimated a total of 1,331 hours per month, an equivalent of 7.69 positions (1,331 hours/173 hours per month). Further, the State estimated that the contracted job would require a total of 173 hours per month for nine total positions, to include other positions, such as project manager, office manager, accountant, financial analyst, etc. However, at 173 hours per month, the winning contractor's proposal estimated nearly 27 total positions needed for the job. In addition, the State could not support that it assessed the personnel cost for the remaining five proposals. Although, the proposal analysis was not completed in accordance with the State's established methodology, we did not question any cost for this procurement due to the competition received and the complete proposals analysis, which included three other factors in addition to staffing cost.²⁶

The Contractor's Eligibility Was Not Assessed in a Timely Manner

The State did not perform a timely review of the excluded parties for the winning contractor's eligibility for the construction management services contract. In accordance with appendix II to 2 CFR part 200 and Executive Order 12549, the State included in its request for proposal an eligibility requirement that any offeror that is debarred, suspended, or otherwise excluded from Federal contracting is ineligible for this procurement. The U.S. General Services Administration's System for Award Management (SAM) database provides information on debarment and suspensions related to Federal contracting. However, the State did not check the database in a timely manner. The State awarded the procurement in May 2019 but did not check the SAM database until September 2019. By retrieving archived data in SAM,²⁷ we confirmed that the contractor was eligible in May 2019. However, the State needed to follow policy and its solicitation and check for eligibility before awarding a contract, thus avoiding the risk of awarding a contract to ineligible vendors.

The State Did Not Fully Understand Procurement Requirements

The State did not fully understand the procurement requirements. NCORR's Director of Recovery and Resiliency stated that an independent cost estimate was the same as a cost or price analysis and that it was up to the grantee to assess the facts surrounding the procurement to determine whether any further

²⁶ For evaluating the proposals received, the State's request for proposal identified a point system comprised of 100 total points possible in four categories: (1) 35 points for technical approach to the scope of work, (2) 10 points for demonstrated ability to comply with all State and Federal requirements, (3) 35 points for relevant qualifications and experience, and (4) 20 points for cost proposed (personnel cost detailed by estimated number and types of positions, number of hours, and hourly rate to provide an estimated monthly cost for the completion of proposed scope of work).

²⁷ Whether these archived data were available to the State was not relevant since the State would have needed to check the database actively during its procurement process. We checked the archived data only to confirm whether the awarded contractor was listed as ineligible when the State awarded the contract.

analysis was warranted. Specific to the procurement of the construction management services contract, discussed above, the Director of Recovery and Resiliency stated that (1) an independent cost estimate, read as “cost analysis,” was completed; (2) a consensus score was made of all received proposals; and (3) the award reasonableness for the selected vendor was additionally supported by the fact that the contract price was in line with other proposals received. As stated above, the State’s memorandum entitled “Cost Analysis” was not an analysis of proposals received but, instead, was the State’s cost estimate for the contract. However, since “cost analysis” is a term used in 2 CFR 200.324,²⁸ the State should refer to its cost estimate as an estimate in its procurement manual to reduce future confusion by its staff and the risk of conflating cost analysis with a cost estimate.

The cost or price analysis is one method for documenting that the costs are reasonable. However, there are components that go into an offered price, which when evaluating the price, the State may or may not have considered. Specifically, the State asked for a detailed staffing plan as part of its solicitation, but from documentation maintained, the State did not use the staffing plan. Instead, the State appeared to have evaluated the proposals received only for unit price, contrary to its cost analysis/cost estimate and its solicitation. If all offerors come in much lower or much higher than the independent cost estimate, the State has the ability to select the best offer. Therefore, a cost estimate is not the same as a cost or price analysis.

Additionally, the State’s policy was not clear in defining an independent cost estimate and price analysis. Regulations under 2 CFR 200.323(a) (December 19, 2014) state that an independent cost estimate must be made as a starting point in connection with every procurement. The State’s procurement policy provided that it was equivalent to Federal regulations at 2 CFR 200.318 through 200.326 (December 19, 2014), but the State’s comparison of its equivalency to Federal requirements did not address 2 CFR 200.323(a) (December 19, 2014) in its entirety. Specifically, it did not consider an independent cost estimate before receiving bids or proposals.²⁹ Further, the State’s procurement policy, dated January 2020 with modified date of March 13, 2020, used the term “cost or price analysis” in describing an independent cost estimate when conducting sole source procurements. By using cost analysis terminology the policy becomes unclear and misleading to the user.

²⁸ The procurement requirements were amended in the 2020 update of the Uniform Guidance (2 CFR 200) thereby affecting the numbering of the regulations. The requirements at 2 CFR 200.324 were listed at 2 CFR 200.323(a) in the previous version (December 19, 2014).

²⁹ Regardless of HUD’s approval of the State’s comparison, the effect of the State’s procurement process and standards was required to be equivalent to the effect of procurements under CFR 200.318 through 200.326 (December 19, 2014).

Conclusion

Because the State did not follow its disbursement procedure and did not fully understand procurement requirements, it could not support that it obtained adequate invoice documentation for issuing payments and prepared independent cost estimates before the bidding process, properly assessed the cost reasonableness of contracts, and assessed contractor eligibility in a timely manner. As a result, the State could not provide reasonable assurance to HUD that more than \$2.5 million in CDBG-DR funds was spent properly.

Recommendations

We recommend that the Deputy Assistant Secretary instruct the State of North Carolina to

- 1A. Provide adequate documentation to support that the \$2,588,362 in CDBG-DR funds for three unsupported project and program management services expenditures cited in this report was spent for supported, necessary, and reasonable costs. Any amount for which adequate support cannot be provided should be repaid from non-Federal funds.
- 1B. Update its procurement policy to clearly define the process, which includes timing and the procurement types, for conducting an independent cost estimate and a price analysis.
- 1C. Provide training to State staff to ensure that it understands and follows (1) requirements to maintain adequate documentation to support that program disbursements are eligible and reasonable and (2) procurement requirements, including independent cost estimates, cost analyses, proposal scoring, and the timely checking of the SAM data for contractors' eligibility.

Scope and Methodology

We performed our fieldwork at the North Carolina Department of Commerce at 301 North Wilmington Street, Raleigh, NC, the North Carolina Office of Recovery and Resiliency at 200 Park Offices, Morrisville, NC, and in our offices in Greensboro, NC, and Atlanta, GA. We conducted our audit work from May 2019 through March 2022. Our audit period was December 10, 2016, through March 22, 2022.

To accomplish our audit objective, we interviewed Commerce and NCORR³⁰ personnel and HUD officials. In addition, we obtained and reviewed the following:

- Relevant laws, regulations, and program guidance.
- The State's policies and procedures with focus on financial management and procurement, organizational chart, disaster recovery staffing plans, CDBG-DR general ledger, bank statements, and interagency agreement with the North Carolina Office of State Budget and Management.
- The State's procurement documentation and expenditure files.
- The State's CDBG-DR Hurricane Matthew action plan and amendments.
- The State's grant agreement, dated August 15, 2017, and March 15, 2018 (amended).
- HUD's monitoring reports, dated November 6, 2018, July 18, 2019, and August 14, 2020.
- HUD's Disaster Recovery Grant Reporting (DRGR) system³¹ reports.
- The U.S. General Services Administration's SAM) database.

To determine whether the State followed requirements related to the disbursement of its CDBG-DR funds, we selected and reviewed a nonstatistical sample of expenditures processed by both NCORR and Commerce. Specifically, using financial reports in DRGR, we randomly selected and reviewed 14 expenditures totaling more than \$2.3 million from a universe of 54 expenditures totaling nearly \$12 million processed by NCORR between July and September 2019. Further, we used Commerce's CDBG-DR general ledger to select a sample of 11³² expenditures totaling more than \$3.1 million from a universe of 89 expenditures totaling more than \$8.5 million that were processed between May 2018 and May 2019. This resulted in a total sample of 25 expenditures reviewed from a total universe of 143 expenditures processed by NCORR and Commerce. We were unable to use the information from DRGR to select a sample of expenditures processed by Commerce because of its filing system. Commerce's records were paper copies filed in the order of vendors and not in the order of drawdowns completed in DRGR,³³ while NCORR's records were electronic and easily searchable. The use of DRGR or the general ledger did not have a significant impact in our sample selection because we were able to review support documentation maintained by NCORR and Commerce to sufficiently accomplish our audit objective. We did not review 100 percent of expenditures. Although this approach did not allow us to project the results of the sample to the population, it was sufficient to meet the audit objective.

³⁰ The State's department responsible for administering the CDBG-DR funds was changed from Commerce to NCORR. See the Background and Objective section of this report for details.

³¹ The DRGR system is primarily used by grantees to access grant funds and report performance accomplishments for grant-funded activities.

³² Our selection of 11 expenditures included 9 random selections and 2 judgmental selections based on concerns identified by Commerce's staff during interviews.

³³ The method for paying its vendors is determined by the grantee and not related to how it completes the drawdowns in DRGR. For example, a grantee can complete one drawdown in DRGR to pay multiple vendors.

To determine whether the State followed procurement requirements related to its CDBG-DR funds, we selected and reviewed a nonstatistical sample of three contracts from a universe of eight contracts procured by NCORR and under Commerce.³⁴ Specifically, between January and September 2019,³⁵ NCORR had procured six of these contracts totaling more than \$66.8 million, of which we selected and reviewed two contracts representing nearly 78 percent (\$51.87 million) of the universe in dollars. These contracts were for program management services and construction management services. We noted deficiencies in both procurements. We determined that the results were sufficient to accomplish our objective and did not warrant reviewing 100 percent of five contracts procured by NCORR. Further, of the two contracts procured under Commerce before January 2019, we selected and reviewed one contract, valued at more than \$16.7 million, which was for project and program services and management. We selected the contract based on local media allegations of impropriety by a State official in awarding the contract.³⁶ We did not review 100 percent of two contracts procured under Commerce. Although this approach did not allow us to project the results of the sample to the population, it was sufficient to meet the audit objective.

We relied in part on computer-processed data contained in the State's system and HUD's DRGR system to achieve our audit objective. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing and found the data to be adequately reliable for our purposes. The tests for reliability included but were not limited to comparing computer-processed data to drawdown support documents, expenditure support documents, and bank statements.

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

³⁴ See footnote 2.

³⁵ As discussed in the Background and Objective section of this report, HUD approved NCORR in July 2019 as the CDBG-DR grantee for the State; however, NCORR had begun disaster recovery efforts, to include awarding procurement contracts, as of January 2019.

³⁶ The media alleged that leaders at the State rewrote a memorandum recommending that a multi-million-dollar contract be awarded to three companies instead of one. While the allegations of impropriety had some merit, we determined that there was no impact because the improper actions were rectified and a contract was not awarded based solely on one State official's decision. However, we noted a compliance deficiency in the procurement, which is discussed in the Results of Audit section of this report.

Appendixes

APPENDIX A – SCHEDULE OF QUESTIONED COSTS


Table 2. Schedule of Questioned Costs


Recommendation number	Unsupported 1/
1A	\$2,588,362
Totals	2,588,362

1/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

APPENDIX B - AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation – Auditee Comments


DEPARTMENT OF PUBLIC SAFETY
Roy Cooper, Governor
Eddie M. Buffalo, Jr., Secretary


NORTH CAROLINA OFFICE OF RECOVERY AND RESILIENCY

NORTH CAROLINA DEPARTMENT OF PUBLIC SAFETY
OFFICE OF RECOVERY AND RESILIENCY
Laura H. Hogshhead, Director

July 15, 2022
Nikita N. Irons
Audit Director
75 Ted Turner Drive SW, Room 330
Atlanta, GA 30303

Dear Ms. Irons –

NCORR appreciates the time and effort that HUD OIG put into finalizing the 2019 draft report of our Hurricane Matthew CDBG-DR program(s). We have reviewed the report and welcome the opportunity to respond, and further explain NCORR's position on the findings outlined.

The first finding we will address is related to the Independent Cost Estimate (ICE) process.

Our position is that the OIG has misinterpreted NCORR's procurement manual as being more stringent than 2 CFR 200, specifically with regards to timing. The certification at the time of the reviewed procurements was done to the State Procurement Rules in the Matthew certification. Under State Procurement rules, there is no requirement to perform an independent cost analysis. When the state procurement rules are silent on an issue of federal procurement rules, then the relevant federal rule applies. The correct policy to apply to an ICE for the NCORR Matthew procurements reviewed would be the federal procurement standard – 2CFR200.323(a).

Based on our understanding of the finding, the OIG has applied the excerpt below from page 18 of the 2019 NCORR Procurement Manual as follows to issue the finding:

B. PRICING

NCORR shall ensure that profit is negotiated as a separate element of price for contracts awarded without competition and, to the extent permissible under state law, profit is negotiated for contracts costing \$250,000 or more where a cost analysis is performed prior to soliciting bids.

This section of NCORR's procurement manual describes the heightened standard of an ICE being performed before "soliciting bids" and is specifically restricted to contracts awarded without competition. The procurements reviewed by the OIG were competitive procurements.

The early requirement of the 2019 NCORR Procurement Manual to perform an ICE before soliciting bids is when it is done for a contract that will be procured from a single, identified vendor. This proper interpretation elucidates why profit would be negotiated separately – it was

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 **Comment 1 >**

 **Comment 2 >**

 **Comment 2 >**

 **Comment 2 >**

 **Comment 2 >**

 **Comments 1 and 2 >**

 **Comments 1 and 2 >**

 **Comment 3 >**

done without competition, and it was done with a donation or special discount where we would purchase something from the grantor. It would make sense in these cases to perform the cost or price analysis before soliciting bids because in one instance it is without competition and in the other it is done where we would purchase something from a specific grantor (i.e., in both places we know we want to purchase something from a single specific entity and therefore the analysis would need to be done beforehand as the other entity is known beforehand). Additionally, the issuance of the proposal under these two scenarios may result in a signed contract within hours and therefore it is apparent why the ICE is performed at this earlier stage.

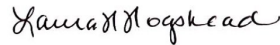
This subject is also touched upon in the Procurement Process Overview on page 21 of the 2019 NCORR Procurement Manual. The same reference and language can be found in the procurement crosswalk too.

It is NCORR's position that the procurements reviewed did not require a cost analysis or ICE before "soliciting bids" per the 2019 NCORR Procurement Manual. The procurement only required that NCORR follow the requirement of performing an ICE before receiving bids, not before soliciting bids.

We hope this explanation assures OIG that an ICE was performed at the correct time during the procurements reviewed. We trust the OIG will agree, given the information above, that this is not a finding.

Regarding the finding identified with costs questioned, it should be noted, this procurement was inherited by NCORR and subsequently, we implemented procurement practices which no longer permit program management as a unit-based charge. Billing documentation requirements have been strengthened and the type of required documents are stronger. NCORR will work diligently to support the payments identified by the OIG.

Sincerely –



Laura H. Hogshead

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OIG Evaluation of Auditee Comments

- Comment 1 The State's position is that OIG misinterpreted its procurement manual to be more stringent than the Federal requirements at 2 CFR 200 with regards to timing of cost estimates. In addition, the State stated that its certification to HUD for Hurricane Matthew disaster recovery funding was done to the State [of North Carolina's] procurement rules, which according to the State were silent on the requirement for conducting an independent cost estimate or cost analysis, to quote the terminology in the State's response letter. Therefore, the rules to apply correctly are the Federal requirements at 2 CFR 200 and not the State's procurement manual.
- The 2019 procurement manual makes no mention of following 2 CFR 200; instead, it provides that the State will follow the procurement rules established by state statutory law. Further, in the 2019 procurement manual, the state certified pursuant to 81 Federal Register 83254, Sec VI.A.1.a that it will follow North Carolina's rules and procedures for any procurement funded by a CDBG-DR grant.
- In addition, the State's position in its polices and practice conflicts with its response position. The State appears to ignore the entirety of its crosswalk related to its certification, which has the purpose of showing to HUD how the Federal and State procurement requirements compare. While its crosswalk stated that the cost estimate or a price analysis is not required under the state law, it certified that "[the State] shall ensure that a cost or price analysis is conducted for all contracts costing \$250,000 or more *prior to soliciting bids*" (emphasis added), which is discussed in the report. However, the crosswalk fails to address how the State will comply with the requirement for an independent cost estimate. We acknowledge that a cost estimate was completed but documented as a cost analysis for one procurement and throughout its procurement manual, it provides that a cost analysis will be done prior to the receipt of proposals or issuance of solicitation. Since it is impossible to analyze cost before the receipt of proposals, the State is unclear on both concepts and the timing of when each is applicable in the procurement process.
- Further, the timing of completing a cost estimate is found in its procurement manual in three places (Section VII(B) on page 18, Section VIII(D)(1)(a), and Section IX on page 21), which is in addition to its crosswalk. However, by using cost analysis terminology the policy becomes unclear and misleading to the user. The State should work with HUD during the audit resolution process to fully implement recommendation 1B.
- Comment 2 The State cited an excerpt from its procurement manual at Section VII(B) as the basis for our finding related to competitive procurements. Specifically, the State stated that the section applies only to noncompetitive procurements. In addition, the State explained Section VIII(D)(1)(a) of its procurement manual that the timing requirement of completing an independent cost estimate before soliciting bids applies for situations where a single, identified vendor is procured that may result in a contract being signed within hours of the solicitation issuance. As such, the State believed that it is apparent why the independent cost estimate is performed prior to soliciting bids. Further, the State acknowledged that the timing of completing a cost estimate is touched upon on page 21 of the 2019 Procurement Manual and found in its crosswalk too.

In addition to its crosswalk, the requirement for completing an independent cost estimate or cost analysis to quote the terminology in the State's policy is found in three places (Section VII(B) on page 18, Section VIII(D)(1)(a), and Section IX on page 21) in the State's procurement manual. While both Sections VII(B) and Section VIII(D)(1)(a) relate to noncompetitive procurements, Section IX and the crosswalk for Hurricane Matthew disaster recovery funding, require the completion of an independent cost estimate without limitation to competitive or noncompetitive procurements. Although we cited Section VIII(D)(1)(a) and not Section VII(B), we have updated the report to change the citation to Section IX and the crosswalk since the finding remains unchanged. The State should work with HUD during the audit resolution process to fully implement recommendation 1B.

Comment 3 The State stated that the procurement where we questioned cost was inherited and that it has implemented practices to no longer permit program management as a unit-based charge on a contract. Further, it stated that it has procurement practices and has strengthened requirements for documentation. However, it will work diligently to support cost questioned by us.

As stated in the report, NCORR did not procure the contract in question; it was North Carolina Department of Public Safety, Division of Emergency Management, the agency responsible for administering CDBG-DR funds for the State at the time of procurement. Further, we acknowledge the State's willingness to support the questioned cost. The State should work with HUD during the audit resolution process to ensure that any cost not supported is reimbursed to the program from non-Federal funds.

APPENDIX C - PROJECT AND PROGRAM SERVICES AND MANAGEMENT CONTRACT (19-RFP-014128-WAX)

Section 4.3 Invoices

1. The vendor must submit one monthly invoice within fifteen calendar days following the end of each month in which work was performed.
2. Invoices must be submitted to the Contract Lead in hard copy on the Contractor's official letterhead stationery and must be identified by a unique invoice number. All invoice backup reports and spreadsheets must be provided in electronic format.
3. Invoices must bear the correct contract number and purchase order number to ensure prompt payment. The vendor's failure to include the correct purchase order number may cause delay in payment.
4. Invoices must include an accurate description of the work for which the invoice is being submitted, the invoice date, the period of time covered, the amount of fees due to the vendor and the original signature of the vendor's project manager.