OFFICE OF AUDIT
REGION 9
LOS ANGELES, CA

City of Hawthorne, CA

Community Development Block Grant Program

2013-LA-1010

SEPTEMBER 20, 2013

Issue Date: September 20, 2013

Audit Report Number: 2013-LA-1010

TO: William Vasquez, Director, Los Angeles Office of Community Planning and Development, 9DD

///SIGNED///

FROM: Tanya E. Schulze, Regional Inspector General for Audit, Los Angeles Region, 9DGA

SUBJECT: The City of Hawthorne, CA, Did Not Administer Its Community Development Block Grant Program Cost Allocations in Accordance With HUD Rules and Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our review of the City of Hawthorne's Community Development Block Grant and Community Development Block Grant-Recovery Act Programs.

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

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

If you have any questions or comments about this report, please do not hesitate to call me at 213-534-2471.

September 20, 2013

The City of Hawthorne, CA, Did Not Administer Its Community Development Block Grant Program Cost Allocations in Accordance With HUD Rules and Requirements

Highlights

Audit Report 2013-LA-1010

What We Audited and Why

We initiated a review of the City of Hawthorne's Community Development Block Grant (CDBG) and CDBG-Recovery Act (CDBG-R) program, based on a request by the U.S. Department of Housing and Urban Development's (HUD) Los Angeles Office of Community Planning and Development. Our objective was to determine whether the City adequately supported its salary and program administrative cost allocations to the CDBG and CDBG-R programs in accordance with HUD requirements.

What We Recommend

We recommend that the Director of HUD's Los Angeles Office of Community Planning and Development require the City to (1) provide adequate support for more than $1.6 million in salary costs or repay the CDBG program from non-Federal funds, (2) repay the program $34,028 in ineligible administration expenses from HOME Investment Partnerships program funds, (3) provide support for $12,733 in administration costs or repay the program from HOME funds, (4) develop written policies and procedures for its salary and administrative allocation, and (5) provide training to CDBG employees on program requirements.

What We Found

The City did not adequately support its cost allocations to its CDBG program activities in accordance with applicable HUD rules and requirements. It was unable to properly support more than $1.6 million in employee salaries allocated to its CDBG program activities, incurred $34,028 in ineligible CDBG program costs, and incurred $12,733 in unsupported CDBG program expenses.

We found no issues with the City's use of its CDBG-R program funds.

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BACKGROUND AND OBJECTIVE

Incorporated in 1922, the City of Hawthorne has a population of nearly 87,000 within a 6-square-mile area. There are several departments that help run the City, including the Planning and Community Development department. Community Development is responsible for administering the Federal Community Development Block Grant (CDBG) and HOME Investment Partnerships Program.

CDBG Program

The CDBG program works to ensure decent, affordable housing, to provide services, and to create jobs through the expansion and retention of businesses. Not less than 70 percent of CDBG funds must be used for activities that benefit low- and moderate-income persons. In addition, each activity must meet one of the following national objectives for the program: benefit low- and moderate-income persons, prevent or eliminate slums or blight, or address community development needs having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community for which other funding is not available. The table below summarizes the funding awarded to the City's CDBG and CDBG-Recovery Act (CBDG-R) programs throughout our audit period.

Program year	IDIS* #	Project activity	Funding
2010	1	Program administration	$291,691
	2	Graffiti removal	$108,427
	3	Crime-free multifamily housing	$108,427
	4	Code enforcement	$449,432
		2010 subtotal	**$957,977**
2011	1	Program administration	$317,746
	7	Graffiti removal	$109,000
	8	Crime-free multifamily housing	$109,000
	9	Code enforcement	$276,963
		2011 subtotal	**$812,710**
2012	2	Program administration	$241,941
	4	Graffiti removal	$109,000
	5	Crime-free multifamily housing	$31,656
	6	Code enforcement	$50,069
		2012 subtotal	**$432,666**
CDBG		Total CDBG	$2,203,353
CDBG-R		Public facilities & improvements - economic development	$459,958
		Total CDBG and CDBG-R	**$2,663,311**

* IDIS = HUD's Integrated Disbursement and Information System

Additionally, HUD last conducted a monitoring review of the City's CDBG program in July 2005. HUD issued findings on the City's code enforcement program regarding eligibility; specifically determining that (1) code enforcement activities were carried out citywide rather

than in deteriorated or deteriorating areas, (2) program activities were carried out in ineligible census tracts (non-CDBG areas) containing less than 51 percent low- and moderate-income persons, and (3) HUD could not determine from code enforcement officer daily logs what percentage of staff time was charged to the CDBG program. The City responded to the findings in December 2005 by defining deteriorated or deteriorating areas using the City's property maintenance ordinance; defining the target areas or census tract or block groups containing a majority of low- and moderate-income residents; and explaining how time was charged to the CDBG program for each code enforcement staff person and how the determination was made, including stating that each code enforcement officer reported actual time spent on CDBG activities daily.

The objective of our audit was to determine whether the City adequately supported its salary and program administrative cost allocations to the CDBG and CDBG-R programs in accordance with HUD requirements.

RESULTS OF AUDIT

Finding: The City Did Not Administer Its CDBG Program Cost Allocations in Accordance With HUD Rules and Requirements

The City did not adequately support its cost allocations to its CDBG program activities in accordance with applicable HUD rules and requirements. Specifically, it

- Did not properly support more than $1.6 million in employee salaries and benefits allocated to its CDBG program,
- Incurred $34,028 in ineligible program administrative costs, and
- Incurred $12,733 in unsupported program administrative costs.

This condition occurred because the City was not sufficiently knowledgeable of HUD requirements and did not maintain adequate written policies and procedures for salary allocation or program administration. As a result, more than $1.6 million in program funds may not have been made available for decent, affordable housing and other services principally for low- and moderate-income persons.

The City Lacked Support for Salary Allocations

The City did not have a sufficient basis for its allocation of employee salaries to its CDBG program activities. A sample review of employee timesheets for the City's CDBG program activities for fiscal years 2011, 2012, and 2013 revealed that the time recorded by employees on their timesheets for CDBG activities directly corresponded to the City's budgeted CDBG salary allocation plans, which are prepared before the fiscal year. Interviews with the City's CDBG staff confirmed that employees recorded their CDBG work time to match the City's budget allocation plan, rather than recording their actual work time. This method of recording and allocating time is contrary to HUD requirements at 2 CFR (Code of Federal Regulations) 225, Appendix B to 2 CFR 225 (8)(h)(4)-(5) (Office of Management and Budget Circular A-87), which call for after-the-fact distributions (see appendix C).

This issue was apparent in the code enforcement program, for which the CDBG hours listed on timesheets matched those on the budgeted allocation plan. Yet the hours on computer system reports showing actual work time and activities did not support or match the time recorded on employee timesheets.

Further, there was no written methodology showing how the City derived the salary allocation percentages for its CDBG activities on its budgeted salary allocation plan. In addition, there were no adjustments made to the allocation to reflect the actual time spent working on CDBG activities. As a result, costs charged to CDBG salaries and associate benefits were considered unsupported. The total unsupported salaries and benefits for all CDBG program activities reviewed (that is, code enforcement, graffiti removal, crime-free multifamily housing, and program administration) amounted to more than $1.6 million ($692,694 for fiscal year 2011, $646,469 for fiscal year 2012, and $288,967 for fiscal year 2013).

The City Incurred Ineligible and Unsupported Costs From Program Administration Expenses

The City incurred $34,028 in ineligible expenses that should have been charged to other programs. Of this amount, $12,445 was paid for administrative contract services to develop a relocation policy manual, which was applied to recent properties for the HOME program. However, the City charged the entire cost to the CDBG program instead of charging the benefited HOME program. Additionally, the City incurred $20,993 in costs for relocation consultant services, reimbursement costs of $95 for travel expenses, and $495 in application fees for HOME and planning activities, respectively, but charged them to the CDBG program. HUD requirements under 2 CFR Part 225 (Office of Management and Budget Circular A-87) Appendix A to Part 225(C)(c) do not allow costs allocable to a Federal award to be charged to another Federal award.

In addition, the City could not support $12,733 in CDBG program expenses. These expenses included

(1) $3,750 for professional contract services to prepare the fiscal year 2010-2011 consolidated annual performance and evaluation report (CAPER),
(2) $910 to advertise the fiscal year 2010-2011 CAPER,
(3) $6,000 for the preparation of the fiscal year 2011-2012 CAPER, and
(4) $2,073 for the implementation of the City's 5-year implementation plan.

These costs should have been allocated between the CDBG and HOME programs in accordance with 24 CFR 570.206(a)(1-4), since the development of these reports provided information for both HUD programs. Instead, the City charged the entire amount to the CDBG program. The City had no written methodology for allocating these types of joint expenses between programs.

The City Was Unaware of Program Requirements

City staff in charge of administering the CDBG program and performing the activities did not have sufficient knowledge of HUD requirements. In addition, the City did not develop a written plan or basis describing how salary allocations were determined for CDBG employees or maintain adequate policies and procedures for program administration.

Conclusion

The City did not adequately support its cost allocations to its CDBG program activities in accordance with applicable HUD rules and requirements. This condition occurred because the City was not sufficiently knowledgeable of HUD requirements and therefore did not maintain adequate written policies and procedures for salary allocation or program administration. As a result, more than $1.6 million in program funds may not have been made available for decent, affordable housing and other services principally for low- and moderate-income persons.

Recommendations

We recommend that the Director of HUD's Los Angeles Office of Community Planning and Development require the City to

1A. Provide adequate supporting documentation for the $1,628,130 in unsupported salary and benefit costs or repay the CDBG program from non-Federal funds.

1B. Repay the CDBG program $34,028 in ineligible administration expenses from HOME program funds.

1C. Provide support for $12,733 in unsupported administration costs or repay the CDBG program from HOME program funds.

1D. Implement adequate written policies and procedures for its salary and administrative allocations to meet applicable HUD rules and requirements.

1E. Provide adequate training to CDBG employees so that the employees have a better understanding and knowledge of administering the CDBG program in accordance with HUD rules and requirements.

SCOPE AND METHODOLOGY

We performed our onsite audit work at the City's main office in Hawthorne, CA, from January 28 to August 6, 2013. Our review generally covered the period July 1, 2010, to December 31, 2012, and was expanded as necessary.

To accomplish our objective, we

- Interviewed pertinent City personnel involved with the administration of CDBG funds and HUD Office of Community Planning and Development program staff;
- Reviewed Integrated Disbursement and Information System (IDIS) performance reports provided by HUD;
- Reviewed City monitoring reports, CDBG funding agreements, consolidated action plans, and CAPERs;
- Reviewed relevant purchasing, financial, and accounting procedures and records;
- Reviewed the City's internal control policies and procedures;
- Reviewed documentation related to the City's CDBG-funded projects;
- Reviewed the City's organizational charts;
- Reviewed the City's audited financial statements for fiscal years 2009, 2010, and 2011; and
- Reviewed applicable CDBG regulations, including CFR references and Office of Management and Budget requirements.

To test CDBG program expenses, we selected a nonstatistical sample. According to HUD's IDIS reports, the universe of total CDBG expenditures that were expended and drawn during our audit period amounted to $4,035,128. The expenditures sampled totaled $1,900,712 ($938,777 + $401,451 + $560,484). The total percentage for each individual fiscal year amounted to 23 percent ($938,777 / $4,035,128) for 2010, 10 percent ($401,451 / $4,035,128) for 2011, and 14 percent ($560,484 / $4,035,128) for 2012. We sampled the program activities with the most CDBG expenditures for each individual fiscal year. Further, each program activity is comprised of several voucher or expenditure amounts, so we chose a specific voucher or expenditure to review in detail (such as supporting documentation, invoices, canceled checks, contracts, etc.) for that program activity. In total, we sampled 47 percent ($1,900,712 / $4,035,128) of the total population of CBDG program expenditures.

We reviewed the City's budgeted salary allocation plans and timesheets for CDBG employees. We reviewed salaries and benefits for the City's CDBG program activities (code enforcement, graffiti removal, crime-free multifamily housing, and program administration) within our audit scope, from July 1, 2010, to December 31, 2012. We requested a nonstatistical sample of employee timesheets for these program activities, to include examples for fiscal years 2011, 2012, and 2013, and compared the time allocated for CDBG activities to the City's budgeted salary allocation spreadsheets on a percentage basis to determine whether CDBG employees recorded actual CDBG work time in accordance with HUD regulations. We determined that further testing of timesheets was unnecessary since City staff confirmed that our observations were consistent City practice.

Additionally, of the $459,958 in CDBG-R funds awarded to the City, we reviewed the entire amount to ensure that expenditures were eligible and supported.

We found that data contained in source documentation provided by the City agreed with data contained in the City's automated expenditure reports. We, therefore, assessed the data to be sufficiently reliable for our use during the audit.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

INTERNAL CONTROLS

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

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

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

Relevant Internal Controls

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

- Effectiveness and efficiency of program operations - Implementation of policies and procedures to ensure that program funds are used for eligible purposes.

- Reliability of financial information - Implementation of policies and procedures to reasonably ensure that relevant and reliable information is obtained to adequately support program expenditures.

- Compliance with applicable laws and regulations - Implementation of policies and procedures to ensure that monitoring, onsite inspections, and expenditures comply with applicable HUD rules and requirements.

We assessed the relevant controls identified above.

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

Significant Deficiency

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

- The City did not maintain sufficient written policies and procedures to ensure that cost allocations were adequately supported in accordance with HUD rules and requirements (finding).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/	Unsupported 2/
1A		$1,628,130
1B	$34,028	
1C		$12,733
Total	**$34,028**	**$1,640,863**

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.

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

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

CITY OF HAWTHORNE

September 11, 2013

Via Facsimile (213) 894-8115, Email (tschulze@hudoig.gov)
& Regular U.S. Mail

Tanya E. Schulze
Regional Inspector General for Audit
U.S. Department, Housing & Urban Development
Office of Inspector General
611 West 6th Street, Suite 1160
Los Angeles, CA 90017

Dear Ms. Schulze:

We write in response to the 'City of Hawthorne CDBG & CDBG-R Finding Outline' provided to us by you.

Comment 1

The City has reviewed the findings and recommendations made in the outline. We are in the process of producing supporting documentation for the $1,628,130 in salary costs flagged by the findings. The new supporting documentation will be generated based on data collected in COMCATE (the City's code enforcement management system) as well as other data maintained by the City. These data sources constitute a contemporaneous record of the activities of City personnel and will allow the City to specifically identify work hours spent on CDBG-eligible activities. An accurate identification of work hours will allow us to calculate and document for HUD the salaries and administrative allocation associated with those hours. We anticipate that it will take us approximately four (4) months to produce the necessary documentation.

Comment 2

Comment 2

We recognize the need for additional training and written procedures to ensure that future submittals documenting salary and administrative allocations meet applicable HUD rules and requirements. We intend to create such written procedures and provide such training to all relevant City staff.

Sincerely,

Michael Goodson
City Manager
City of Hawthorne

OIG Evaluation of Auditee Comments

Comment 1 The City was not able to provide adequate support for its salary allocations during the course of the audit; therefore, the $1.6 million remains unsupported.

Comment 2 The City will have an opportunity to provide additional information to HUD during the audit resolution process to resolve the recommendations.

Appendix C

CRITERIA

2 CFR Part 225 (Office of Management and Budget Circular A-87)
Appendix A to Part 225 - General Principals for Determining Allowable Costs

C. *Basic Guidelines*
3. Allocable costs.
a. A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.
c. Any cost allocable to a particular Federal award or cost objective under the principles provided for in 2 CFR part 225 may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons.

Appendix B to 2 CFR 225(8)(d)(1)-(5) Compensation for personal services

d. Fringe benefits.
(5) The cost of fringe benefits in the form of employer contributions or expenses for social security; employee life, health, unemployment, and worker's compensation insurance (except as indicated in section 22, Insurance and indemnification); pension plan costs (see subsection e.); and other similar benefits are allowable, provided such benefits are granted under established written policies. Such benefits, whether treated as indirect costs or as direct costs, shall be allocated to Federal awards and all other activities in a manner consistent with the pattern of benefits attributable to the individuals or group(s) of employees whose salaries and wages are chargeable to such Federal awards and other activities.

Appendix B to 2 CFR 225(8)(h)(4)and(5) - (Office of Management and Budget Circular A-87)
Compensation for personal services

h. Support of salaries and wages. These standards regarding time distribution are in addition to the standards for payroll documentation.
(4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation which meets the standards in subsection (5) unless a statistical sampling system (see subsection (6)) or other substitute system has been approved by the cognizant Federal agency. Such documentary support will be required where employees work on:
(a) More than one Federal award,
(b) A Federal award and a non-Federal award,
(c) An indirect cost activity and a direct cost activity,
(d) Two or more indirect activities which are allocated using different allocation bases, or
(e) An unallowable activity and a direct or indirect cost activity.

(5) Personnel activity reports or equivalent documentation must meet the following standards:

(a) They must reflect an after-the-fact distribution of the actual activity of each employee,
(b) They must account for the total activity, for which each employee is compensated,
(c) They must be prepared at least monthly and must coincide with one or more pay periods, and
(d) They must be signed by the employee.
(e) Budget estimates or other distribution percentages determined before the services are performed do not qualify as support for charges to Federal awards but may be used for interim accounting purposes, provided that:

(i) The governmental unit's system for establishing the estimates produces reasonable approximations of the activity actually performed;
(ii) At least quarterly, comparisons of actual costs to budgeted distributions based on the monthly activity reports are made. Costs charged to Federal awards to reflect adjustments made as a result of the activity actually performed may be recorded annually if the quarterly comparisons show the differences between budgeted and actual costs are less than ten percent; and
(iii) The budget estimates or other distribution percentages are revised at least quarterly, if necessary, to reflect changed circumstances.

24 CFR 570.200(a)(5) Cost principles.
Costs incurred, whether charged on a direct or an indirect basis, must be in conformance with OMB Circulars A–87, "Cost Principles for State, Local and Indian Tribal Governments…"

24 CFR 570.206(a)(1)-(4) Program Administrative Costs
(a) *General management, oversight and coordination.* Reasonable costs of overall program management, coordination, monitoring, and evaluation. Such costs include, but are not necessarily limited to, necessary expenditures for the following:

(1) Salaries, wages, and related costs of the recipient's staff, the staff of local public agencies, or other staff engaged in program administration. In charging costs to this category the recipient may either include the entire salary, wages, and related costs allocable to the program of each person whose *primary* responsibilities with regard to the program involve program administration assignments, or the pro rata share of the salary, wages, and related costs of each person whose job includes *any* program administration assignments. The recipient may use only one of these methods during the program year (or the grant period for grants under subpart F). Program administration includes the following types of assignments:

(i) Providing local officials and citizens with information about the program;
(ii) Preparing program budgets and schedules, and amendments thereto;
(iii) Developing systems for assuring compliance with program requirements;
(iv) Developing interagency agreements and agreements with sub-recipients and contractors to carry out program activities;
(v) Monitoring program activities for progress and compliance with program requirements;

(vi) Preparing reports and other documents related to the program for submission to HUD;
(vii) Coordinating the resolution of audit and monitoring findings;
(viii) Evaluating program results against stated objectives; and
(ix) Managing or supervising persons whose primary responsibilities with regard to the program include such assignments as those described in paragraph (a)(1)(i) through (viii) of this section.

(2) Travel costs incurred for official business in carrying out the program;

(3) Administrative services performed under third party contracts or agreements, including such services as general legal services, accounting services, and audit services; and

(4) Other costs for goods and services required for administration of the program, including such goods and services as rental or purchase of equipment, insurance, utilities, office supplies, and rental and maintenance (but not purchase) of office space.