



**Office of Community Planning and Development
Washington, DC**

**Community Development Block Grant, Section
108, Economic Development Initiative, and
Brownfield Economic Development Initiative
Programs**



Issue Date: February 28, 2014

Audit Report Number: 2014-LA-0001

TO: Yolanda Chavez, Deputy Assistant Secretary for Grant Programs, DG

//SIGNED//

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

SUBJECT: CPD Did Not Monitor Grantees' CPD-Funded Assets Transferred by Former Redevelopment Agencies To Minimize HUD's Risk

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Office of Community Planning and Development's (CPD) monitoring of CPD-funded assets transferred by former redevelopment agencies.

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 8M, 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.



February 28, 2014

CPD Did Not Monitor Grantees' CPD-Funded Assets Transferred by Former Redevelopment Agencies To Minimize HUD's Risk

Highlights

Audit Report 2014-LA-0001

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD) San Francisco and Los Angeles Offices of Community Planning and Development's (CPD) monitoring of CPD-funded assets transferred by former redevelopment agencies due to concerns that CPD-funded assets may be lost during the State of California's statewide mandated closure of redevelopment agencies. Our objective was to determine whether the San Francisco and Los Angeles CPD field offices monitored grantees' CPD-funded assets transferred by former redevelopment agencies to minimize HUD's risk.

What We Recommend

We recommend that HUD (1) develop policies and procedures that allow for more proactive monitoring of grantees' CPD funding and assets, (2) establish a formal listing of assets funded through CPD, and (3) require its grantees to provide adequate documentation supporting the grantees' binding and enforceable rights to CPD-funded assets as required in HUD regulations and requirements.

What We Found

The San Francisco and Los Angeles CPD field offices did not monitor grantees' CPD-funded assets transferred by former redevelopment agencies to minimize HUD's risk. Further, the CPD offices did not record and maintain accurate and complete lists of grantees' CPD-funded assets or track CPD-funded assets managed by the grantees' former redevelopment agencies during the State's mandated shutdown of the agencies. Therefore, there was no assurance that CPD had a complete and accurate account of CPD-funded assets. As a result, more than \$99 million in CPD funds used to acquire assets by the defunct redevelopment agencies is at risk of being transferred to entities that may not continue to meet HUD's CPD program objectives.

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BACKGROUND AND OBJECTIVE

As part of the State of California's budget deficit resolution, the governor issued an executive action to close all redevelopment agencies. The executive order established a deadline of February 1, 2012, for California cities with redevelopment agencies to close down and then transfer all assets to designated receivers (successor agencies). As part of the executive order, each successor agency must submit to the State's Oversight Board and Finance committee a long range property management addressing the use and disposition of the former redevelopment agency's assets. The options include 1) the retention of the asset for governmental use pursuant to State regulation, 2) the retention of the asset for future development, 3) the sale of the asset, or 4) the use of the asset to fulfill an enforceable obligation. Before the executive order, several redevelopment agencies managed U.S. Department of Housing and Urban Development (HUD), Office of Community Planning and Development (CPD)-funded assets on behalf of the respective cities. Further, HUD awarded grantees CPD funds, such as Community Development Block Grant (CDBG), Section 108 Loan Guarantee, Economic Development Initiative (EDI), and Brownfield Economic Development Initiative (BEDI), to pass through to at least 90 redevelopment agencies in California to meet each of the programs' specific objectives and goals.

Grantees use CDBG funds to develop viable urban communities by providing decent housing and a suitable living environment and by expanding economic opportunities, principally for low- and moderate-income persons. The Section 108 program is the loan guarantee provision of the CDBG program that provides grantees with a source of financing for economic development, housing rehabilitation, public facilities, and large-scale physical developments. EDI grants are used to directly enhance the security of Section 108 guaranteed loans or to improve the viability of the same Section 108-assisted project. BEDI is a key competitive grant program that HUD administers to stimulate and promote economic and community development with the redevelopment of abandoned, idled, and underused industrial and commercial facilities where expansion and redevelopment are burdened by real or potential environmental contamination. Without the grantees' having ownership of these CPD-funded assets, there are risks of physically losing assets that could generate future program incomes, add to the affordable housing stock, or generate other future economic and community development opportunities for the targeted areas.

Since redevelopment agencies have closed or are in the process of closing, there are concerns that affordability covenants related to CPD-funded assets may be ignored during the transfer of control. Additionally, there are concerns that CPD or the redevelopment agencies did not maintain adequate documentation of the CPD-funded assets or funds. The State's fiscal issues, which led to its sale of State-owned assets, raise significant concerns that CPD-funded assets may be included in these sales without CPD approval. As a result, there is a possibility that undisclosed sums of CPD funds may go unaccounted for or be lost during the transfer from the redevelopment agencies to successor agencies. Further, these successor agencies may ignore HUD requirements and regulations and assume that no CPD funds were associated with the related assets. Finally, these funding issues, from a Federal perspective, raise concerns that CPD may not have the necessary resources to monitor the actions taking place in California. Therefore, potential limited resources may hamper CPD's ability to ensure that its interests are

protected and risks are minimized during the State's mandated shutdown of redevelopment agencies and transfer of CPD-funded assets.

Our objective was to determine whether the San Francisco and Los Angeles CPD field offices monitored grantees' CPD-funded assets transferred by former redevelopment agencies to minimize HUD's risk.

RESULTS OF AUDIT

Finding: CPD Did Not Monitor Grantees' CPD-Funded Assets Transferred by Former Redevelopment Agencies To Minimize HUD's Risk

The San Francisco and Los Angeles HUD CPD field offices did not record and monitor CPD-funded assets that were part of the State's mandated shutdown of grantees' redevelopment agencies. These field offices relied on the grantees to provide information about the affected assets. However, such information was not available since the grantees did not have the required documentation to support ownership of the sampled assets. This condition occurred because CPD's lack of formal policies and procedures and controls for monitoring did not ensure that CPD-funded assets' interests were maintained and at an acceptable risk. The associated risk of grantees' not having ownership of these CPD-funded assets includes the physical loss of assets that could generate future program incomes, add to the affordable housing stock, or generate other future economic and community development opportunities for the targeted areas. Without policies in place, CPD-funded assets may not continue to meet program objectives. As a result, at least \$99 million in CPD funds used to acquire assets by the defunct redevelopment agencies is at risk of being transferred to entities that may not continue to meet CPD program objectives.

San Francisco and Los Angeles Field Offices Did Not Monitor the Transfer of CPD-Funded Assets

The San Francisco and Los Angeles CPD field offices did not monitor grantees with respect to CPD funds spent on redevelopment assets. In addition, neither office had complete and accurate information readily available to identify affected assets and programs overseen by the defunct redevelopment agencies. Instead, CPD staff relied on the grantees for information that they should have maintained for monitoring purposes. CPD staff acknowledged that there was a hands-off approach to monitoring the transfer of assets from the grantees' redevelopment agencies to designated successor agencies. Without a comprehensive approach, there is a risk that CPD-funded assets may be lost during the closure process of the former redevelopment agencies.

The San Francisco field office provided a list of assets that pertained only to Section 108 rather than a complete list of CPD-funded assets impacted by the redevelopment agency closure. Further, the field office had not reviewed whether assets were properly transferred by the redevelopment agencies to the respective successor agencies.

The Los Angeles field office provided a list of grantees with the respective redevelopment agencies. Discussions with Los Angeles field office staff revealed that the field office did not maintain a list of grantees' assets.

The Los Angeles field office indicated that CPD-funded assets managed by its grantees' redevelopment agencies were not tracked and monitored for accuracy in identifying and transferring the affected assets to the successor agencies. In addition, field office staff relied on the grantees for information about the CPD-funded assets. The Los Angeles CPD field office did not monitor the use of the grantees' funding for the acquisition and construction of these assets. CPD staff confirmed that the field office did not monitor its' grantees to ensure that all of HUD regulations and requirements were met due to limited resources. Consequently, CPD's reliance on the grantees, without formal and proactive monitoring to ensure ownership of the grantees' assets, created uncertainty regarding whether CPD-funded assets would continue to meet CPD program objectives.

Grantees Did Not Have Binding and Enforceable Rights to Sampled Assets

Since the CPD field offices essentially relied on the grantees to ensure that CPD-funded assets were properly identified and transferred from the former redevelopment agencies to the successor agencies, we reviewed and sampled 20 assets from the Cities of San Francisco, San Jose, and Los Angeles to determine whether that had occurred. In 15 of 20 assets reviewed, the grantees did not have the required documentation to show binding and enforceable rights to these assets. 10 of the 15 assets were subject to the State's dissolution process.

Seven of the ten sampled assets reviewed for the cities of San Francisco and San Jose combined were subject to the State's dissolution process. Without these grantees having binding and enforceable rights to the reviewed assets, there was no assurance that CPD program objectives, including economic development and affordable housing, would continue to be met as required by 24 CFR (Code of Federal Regulations) 570.503(b)(7) (see appendix D).

Discussions with the City of San Francisco confirmed that the grantee was not the owner or beneficiary of any of the four reviewed CPD-funded assets managed and administered by the City's former redevelopment agency. The City was unable to provide documentation that showed binding and enforceable rights that ensured that the former redevelopment agency used the reviewed assets in accordance with program requirements. Further, the City's affected assets were subject to the State's dissolution process, which would require it to request that the State transfer the assets in question to its control.

The City of San Jose did not obtain ownership and control of three of the assets sampled during the review. Instead, private developers that conducted business with the defunct redevelopment agency were listed as the owners and beneficiaries of the assets in question. Further, the City could not ensure that it would continue to meet specific program objectives in the areas of economic development and affordable housing as required by 24 CFR 85.42, 570.705, and 570.506(d) without binding and enforceable rights to these CPD-funded assets. As a result, more than \$38 million in CPD program funds may be lost.

Below is a listing of CPD-funded assets that the Cities of San Francisco and San Jose did not have documentation to show binding and enforceable rights.

Grantee	Project	HUD funding amount
San Francisco	Bayview Hunters Point	\$4,000,000
San Francisco	Yerba Buena Center – Marriott	\$20,087,385
San Francisco	Yerba Buena Center – Metreon	\$2,142,569
San Francisco	Yerba Buena Center – Howard Street	\$6,704,961
San Jose	Masson: 161 W. Santa Clara Street	\$1,500,000
San Jose	Security: 84 S. First Street	\$2,350,000
San Jose	EU: 35 & 49 E. Santa Clara Street	\$1,350,000
Total		\$38,134,915

See appendix C for a listing, photos, the status, and the type of funding related to the CPD-funded assets affected by the State-mandated shutdown of redevelopment agencies that the Cities of San Francisco and San Jose could lose by not having documentation to show binding and enforceable rights.

For the Los Angeles CPD field office, 8 of the 10 sampled assets totaling more than \$61 million in CPD program funds did not have the required documentation to show that the City of Los Angeles had binding and enforceable rights as required under the CPD program. 4 of the 10 sampled assets were subject to the State’s dissolution process. These purchases were made to assist the City in meeting specific program objectives that included economic development and affordable housing. However, a public records search identified the City’s defunct redevelopment agency and private developers as the owners of the eight assets in question. Discussions with City officials determined that the City was unable to show that it owned the sampled assets. Further, the City was unable to provide assurance that it had documentation that showed binding and enforceable rights to these CPD-funded assets. As a result, a designated oversight board will oversee the former redevelopment agency’s assets and will be responsible for the potential dissolution of these assets. Without these binding and enforceable rights, it could not ensure that CPD program objectives in the areas of economic development and affordable housing would continue to be met.

Below is a listing of CPD-funded assets that the City did not have the required documentation to show binding and enforceable rights.

Grantee	Project	HUD funding amount
Los Angeles	Marlton Square	\$20,875,000
Los Angeles	The Noho Commons Project	\$18,800,000
Los Angeles	Slauson Central Shopping Center	\$7,658,000
Los Angeles	Goodyear Tract Brownfields Demonstration Site	\$4,442,000
Los Angeles	Goodyear Tract Land Acquisition	\$2,564,068
Los Angeles	Crenshaw Gateway	\$2,218,128
Los Angeles	Blossom Plaza	\$2,599,800
Los Angeles	Westlake Theatre	\$2,000,000
Total		\$61,156,996

See appendix C for a listing, photos, the status, and the type of funding related to the CPD-funded assets affected by the State-mandated shutdown of redevelopment agencies that the City could lose by not having documentation to show binding and enforceable rights.

Conclusion

CPD did not monitor the transfer of grantees' CPD-funded assets transferred by the former redevelopment agencies to minimize HUD's risk. Further, it did not record and maintain accurate records of grantees' CPD-funded assets managed by the respective former redevelopment agencies. Despite this being a significant, unique event, CPD did not take proactive measures to establish specific policies and procedures or implement those in place to address the State's action to close down redevelopment agencies that managed, administered, or owned assets funded with CPD program funds, such as CDBG, Section 108, EDI, and BEDI, among other non-HUD-funded assets. CPD acknowledged that there was a hands-off approach to monitoring the transfer of assets from the grantees' redevelopment agencies to designated successor agencies, based on direction from CPD headquarters. Consequently, CPD did not have a complete and accurate account of CPD-funded assets impacted by the closure of the redevelopment agencies. Further, more than \$99 million in CPD funds used to acquire assets by the defunct redevelopment agencies is at risk of being transferred to entities that may not continue to meet specific CPD program objectives.

Recommendations

We recommend that the Deputy Assistant Secretary for Grant Programs

- 1A. Require all grantees in the State of California to provide adequate documentation, such as title deeds, supporting grantees' enforceable rights to CPD-funded assets as required in HUD regulations at 24 CFR 570.503, 705, and 506, and 24 CFR 85.42. If the grantees are unable to provide required supporting documentation to show binding and enforceable rights to the CPD-funded assets, HUD should implement appropriate administrative action to correct the identified deficiency or recover those funds. This measure would ensure that at least \$99,291,911 in CPD funds could be put to better use in continuing to meet CPD program objectives, which include providing affordable housing and economic development to targeted areas.
- 1B. Develop and implement formal policies and procedures that allow for more proactive monitoring of grantees' CPD funding and assets to ensure that CPD has a plan of action to address this event, as well as possibly similar events in the future, to better ensure that its grantees and subgrantees meet CPD program requirements and funding objectives.
- 1C. Establish a process to ensure that CPD maintains formal listings of assets funded through its CPD programs to ensure better comprehensive awareness and monitoring of its grantees.

SCOPE AND METHODOLOGY

We conducted our audit work at the HUD Office of Inspector General (OIG) in Los Angeles, CA, with site visits to the cities of San Jose, San Francisco, and Los Angeles, between April and November 2013. Our audit period covered the period January 1, 2011, to December 31, 2012.

To accomplish our objective, we

- Reviewed applicable requirements and regulations, policies and procedures, HUD handbooks, guidance, and internal controls relating to the monitoring of CPD-funded assets;
- Interviewed HUD CPD field office staff responsible for the monitoring of grantees' CPD-funded assets;
- Obtained, reviewed, and analyzed assets obtained by grantees' respective redevelopment agencies;
- Conducted site visits to sampled defunct redevelopment agencies' CPD-funded assets; and
- Conducted a public records search of sampled defunct redevelopment agencies' CPD-funded assets.

To determine whether the San Francisco and Los Angeles CPD field offices monitored grantees' CPD-funded assets transferred by former redevelopment agencies to minimize HUD's risk, we selected the largest funded grantees managed by each respective office. For the Los Angeles field office, we determined a universe of 90 grantees with respective redevelopment agencies. We randomly selected five grantees to review; however, four of the five grantees either had minimal CDBG funding or no redevelopment agency that managed its CDBG, Section 108, EDI, and BEDI funding and assets. We relied on HUD's funding matrix, which is comprised of data from HUD's IDIS computer data system, to determine total funding for grantees. We confirmed total funding amounts with the Line of Credit Control System (LOCCS) and determined that the information was reliable for audit purposes. As a result, we selected the remaining sampled grantee, the City of Los Angeles, for review. We then selected 10 assets with the highest funding to review.

For the San Francisco field office, we determined a universe of 73 grantees with redevelopment agencies. We selected the two highest funded grantees with redevelopment agencies for review, the City of San Francisco and the City of San Jose. For the City of San Francisco, we selected the four highest funded assets for review. For the City of San Jose, we selected all six assets for review. We relied on HUD's funding matrix, which is comprised of data from HUD's IDIS computer data system, to determine total funding for grantees.

Audit results were determined through analysis of documentation and site visits. We did not project our findings to the population using this sample.

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

INTERNAL CONTROLS

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

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

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

Relevant Internal Controls

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

- Policies and procedures implemented to ensure that CPD-funded assets meet specific CPD program objectives, which include providing economic development and affordable housing to targeted areas.

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 significant deficiency:

- CPD did not have policies, procedures, and controls in place to ensure that HUD's interests in CPD-funded assets were maintained to meet CPD program objectives, as well as minimize the associated risk of grantees' not having the required documentation to show binding and enforceable rights to these CPD-funded assets, including the potential loss of assets that could generate future program incomes, add to the affordable housing stock, or generate other future

economic and community development opportunities for the targeted areas (finding).

APPENDIXES

Appendix A

SCHEDULE OF FUNDS TO BE PUT TO BETTER USE

Recommendation number	Funds to be put to better use 1/
1A	\$99,291,911

- 1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, the funds to be put to better use totaled more than \$99 million (\$38,134,915 + \$61,156,996 as shown in the finding tables) in CPD-funded assets of which the sampled grantees did not have the required documentation to show binding and enforceable rights during the State-mandated shutdown of redevelopment agencies to ensure HUD's continued interest in meeting its CPD program objectives of providing affordable housing and economic development to targeted areas in need of urban renewal. Implementation of better policies, procedures, monitoring, and controls will help minimize instances of such assets being used for purposes that do not meet HUD's interests in areas such as affordable housing and economic development in targeted areas.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-7000

OFFICE OF COMMUNITY PLANNING
AND DEVELOPMENT

Memorandum

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

From: Yolanda Chavez
Deputy Assistant Secretary for Grant Programs, DG

CC: Maria Cremer, William Vasquez, Stan Gimont, Jessie Kome

Subject: Draft Report
CPD's Monitoring of CPD-Funded Assets Transferred by Former Redevelopment
Agencies

Date: January 31, 2014

Thank you for the opportunity to comment on this draft audit report. CPD takes its role as a steward of public funds seriously and appreciates the opportunity to respond.

Draft Audit Recommendations

The draft report makes three recommendations:

1A. Require all grantees in the State of California to provide adequate documentation, such as title deeds, supporting grantees' enforceable rights to CPD-funded assets as required in HUD regulations at 24 CFR 570.503,505, and 506, as well as 24 CFR 85.31 and 42. If grantees are unable to provide required supporting documentation to show ownership of the CPD-funded asset, HUD should implement appropriate administrative action to correct deficiency and recover those funds. This measure would ensure that at least \$99,291,911 in CPD funds could be put to better use in continuing to meet CPD program objectives, which include providing affordable housing and economic development to targeted areas.

1B. Develop and implement formal policies and procedures that allow for more proactive monitoring of grantees' CPD funding and assets to ensure that CPD has a plan of action to address this event, as well as possibly similar events in program requirements and funding objectives.

1C. Establish a process to ensure that CPD maintains formal listings of assets funded through its CPD programs to ensure better comprehensive awareness and monitoring of its grantees.

CPD strongly disagrees with the three recommendations because they are based on a misunderstanding of HUD program regulations and are therefore incorrect (1A and 1C); and because CPD already has a proactive monitoring process based on an annual risk assessment of its grantees (1B). Moreover, the HUD-OIG (Region 4) audited CPD's Grant Risk Assessment

Comment 1
Comment 2

Comment 3

Procedures (as they relate to subrecipient involvement in CPD programs) in July 2013 and made no recommendations. In addition, our discussion below on the City of Los Angeles projects identified in your audit clearly demonstrates that our risk assessment and monitoring process are effective in identifying problem projects. Additionally, our disbursement and reporting system is adequate in tracking and monitoring all projects funded with CPD funds. Instead CPD is proposing to take the following actions:

1. CPD will review the San Jose and San Francisco projects identified in the audit and provide a status report by September 30, 2014;
2. CPD will continue to monitor its grantees based on its approved monitoring handbook and risk assessment procedures. The Los Angeles and San Francisco Field offices are scheduled to monitor the following grantees in the FY 2014:

Los Angeles Field Office	San Francisco Field Office
City of Bakersfield	City of Turlock
City of Camarillo	City of Hayward
City of Carson	City of Palo Alto
City of El Cajon	City of South San Francisco
City of Huntington Beach	City of Davis
City of Irvine	City of Vacaville
Kern County	City of Woodland
City of La Mesa	City of Concord
City of Lancaster	City of Fremont
City of Los Angeles	City of Livermore
Los Angeles County	City of Pittsburg
City of Lynwood	City of Yuba
City of Montebello	City of Antioch
City of Moreno Valley	City of Citrus Heights
City of Palm Desert	City of Alameda
City of Redlands	City of Clovis
City of Redondo Beach	City of Madera
City of San Clemente	City of Pleasanton
City of San Diego	City of Salinas
San Luis Obispo County	City of Sunnyvale
City of Santa Clarita	City of Reno
City of Temecula	City of San Mateo
City of Thousand Oaks	City of Santa Cruz
City of Tustin	County of Monterey
City of Vista	City of Henderson
City of West Covina	City of Chandler
	City of Phoenix
	City of Peoria
	State of California
	State of Arizona
	State of Nevada

Comment 4

Dissolution of California Redevelopment Agencies (RDAs)

First, it is important to note that HUD had no role in the dissolution of California's almost 400 redevelopment agencies. The dissolution of these agencies was the result of a hard fought budget battle between the Governor and local jurisdictions over control of tax increment dollars generated by the designated redevelopment areas. The Governor wanted these funds to fill the gap in the State's budget deficit. The ultimate decision, which local jurisdictions did not expect, was made by the California Supreme Court when it upheld the Legislature's authority to dissolve these agencies on December 29, 2011. Following the court's decision, the Governor issued an executive order requiring local jurisdictions to select successor agencies to the RDAs and made the shutdown effective February 1, 2012.

Immediately following the court decision, HUD program offices and the Office of General Counsel (OGC) counterparts started meeting regularly to assess potential risks to HUD-funded assets. The CPD field offices contacted all California grantees to assess their successor agency process/decisions, and monitored these closely. CPD Headquarters developed a list of all Section 108 loans that had been guaranteed by tax increment funds or other RDA guarantees. On March 28, 2012, two months after the Governor's executive order took effect, a HUD delegation comprised of the PIH GDAS, CPD DAS for Grant Programs, the Region 9 HUD Administrator, and HUD OGC, met with the State Office of Finance in Sacramento, California, to ensure that the State understood that RDAs served as subrecipients to HUD grantees and that our grantees would be requesting repayments on all federal obligations that had been guaranteed by RDAs in their subrecipient role. CPD has continued to provide technical assistance to grantees as they request repayments on required obligations, including, as necessary, intervening on their behalf with the State Office of Finance.

Draft Audit Report Incorrect References/Misunderstanding of HUD Program Regulations

Comment 5

As stated above, this audit's recommendations are based on a misunderstanding of HUD program regulations. First, the draft audit report includes a number of incorrect references to program regulations. Pages Page 7, 8, and 21 cite to 24 CFR 85.31 as a CDBG program requirement. This provision is not listed as one of the applicable uniform administrative requirements in 570.502. Also, the audit refers to 570.505 as if it applies to all assets – it only applies to real property within the *recipient's* control. 570.503(b)(7) applies to assets within the subrecipient's control.

Comment 6

Therefore, the finding that the San Francisco and Los Angeles field offices did not monitor the transfer of CPD-funded assets implies that CPD had a duty to monitor the assets under the control of subrecipients, which is inconsistent with HUD regulations. Pages 5 and 6 of the audit notes that grantees were relied on for information on CPD-funded assets and to ensure that assets would continue to meet CPD program requirements (as opposed to HUD maintaining information and conducting monitoring on its own).

As we have stated numerous times, our grantees are responsible for all funding they allocate to subrecipients (the RDAs in this case). This is consistent with 570.501, which makes recipients (state and local governments) responsible for ensuring that CPD funds are used in accordance with program requirements. This is also consistent with 570.900(b) (related to performance

review procedures), which states that “HUD will primarily rely on information obtained from the recipient’s . . .,” among other sources of data. This provision also states that “[a] recipient’s failure to maintain records in the prescribed manner may result in a finding that the recipient has failed to meet the applicable requirements to which the records pertain.”

Comment 7

Further, the finding that grantees did not obtain ownership of sampled assets does not recognize that grantees may not have been required to receive ownership of assets. Depending on the program project or deal structure, these assets may be privately owned. In addition, on pages 6 and 7, the audit notes that the cities of San Francisco, San Jose, and Los Angeles did not have documentation to support ownership and control of assets. This finding asks the incorrect question. HUD regulations permit grantees to provide support to subrecipients, who would then maintain ownership or control of assets consistent with the subrecipient agreement. A better question would be whether the city had a subrecipient agreement in place with each RDA subrecipient, and whether that agreement contained provisions required in 570.503(b)(7) related to reversion of assets. It is not apparent from the draft audit that you asked grantees for copies of subrecipient agreements to see whether grantees enforced the terms of those agreements. Subrecipient agreement could potentially be used by the successor agency to put the asset on its Required Obligation Payment Schedule (ROPS) to the State and seek approval for asset transfer to the grantee.

Comment 8

Moreover, depending on the eligible activity, the subrecipient may not have been required to return the asset. For example, economic development activities pursuant to 24 CFR 570.203(b) provide assistance to a for profit business, and subrecipients that directly assisted for profit businesses, even if the business acquired an asset with the CDBG funds, would not be required to return the asset. In this assistance structure, a key question to ask is whether the subrecipient had an agreement with each assisted business including required elements.

Review of City of Los Angeles Projects Confirm Incorrect Conclusions in Draft Audit

Comment 9

CPD’s review of the City of Los Angeles projects identified in the report re-affirms the audit’s misunderstanding of HUD program regulations. Two of the projects, the Goodyear Tract and Blossom Plaza were identified in a previous IG audit, “HUD Need to Improve Its Use of IDIS to Oversee its CDBG Program.” Based on this audit, CPD had already addressed the Goodyear project with the grantee. The Goodyear Tract project is currently moving forward. Remediation work associated with the Brownfields grant the City received for the project has been completed and two portions of the project, Slauson Central and Avalon are currently under construction. In addition, the Goodyear tract is currently part of IG audit 2012-LA-1005, which is in the process of being resolved.

Blossom Plaza was also identified in a CPD 2011 monitoring, along with the Westlake Theatre and Marlton Square. Corrective actions for all three projects are due in July 2014. If the grantee cannot provide evidence that these projects are moving forward, repayment of the CDBG investment will be required.

Comment 10

The City of Los Angeles submitted its claim for the Crenshaw Gateway property, (one would assume based on an executed subrecipient agreement or loan agreement), in January of 2012 and is waiting on the State's approval on the property transfer.

Comment 11

Finally, the Slauson Central Shopping Center project is moving forward. Construction began in 2013 and the City is working with HUD to amend the HUD contract and with the developer on loan terms. The anchor tenant is scheduled to hire 100 people in June 2014.

As stated in our recommendation above, we did not have time to review the San Jose and San Francisco projects, but will do so and provide an update on these projects as well.

Other corrections to the draft Report

Comment 12

On page 10 of the draft audit, you state that the audit period covered January 1, 2011, to December 31, 2012. It is not clear what activities would be covered during 2011, since the RDA dissolution was not effective until February 1, 2012. Moreover, given the nature and complexity of the dissolution process (which continues to evolve), it is shortsighted to assume that final decisions and/or processing of RDA investments would be completed in eleven months after the effective date of the dissolution.

Comment 13

Finally, the audit findings throughout the report (although incorrect) should indicate that they are limited to the 20 projects sampled. As drafted, the findings appear to encompass all CPD monitoring and reporting practices, rather than just the sampled projects.

OIG Evaluation of Auditee Comments

- Comment 1** We agree that CPD has a monitoring process based on an annual risk assessment of its grantees. However, CPD did not have formal policies and procedures, such as a notice, to provide guidance to the field offices and grantees on how to address the State's mandated action to close redevelopment agencies that were tasked with meeting CPD program objectives on behalf of the grantees. This action occurred outside of normal review process and CPD should have directed its efforts to ensure that grantees are able to meet program objectives with minimal effect from the State's actions. As result, we based our recommendations on our assessment of CPD's response to the State's action to dissolve the redevelopment agencies tasked to complete the program objectives on the grantees' behalf. The cited report, 2013-AT-0002, was based on the review of CPD's risk assessment process, or methodology, used for monitoring selected grantees for the fiscal year. Our review specifically focused on how CPD handled the State's actions against redevelopment agencies that acted on behalf of grantees to meet program objectives.
- Comment 2** We did not review the effectiveness of CPD's annual risk assessment and monitoring of grantees during the fiscal year. Instead, our review focused on how CPD responded to the State's action against agencies that were tasked to perform service on behalf of the grantees. Based on discussions with the San Francisco and Los Angeles field office personnel, there was a "hands-off" approach to addressing the issue. Further, CPD headquarters instructed the field offices to assist the State only when requested. These field offices relied on the grantees to enter information about the project status into CPD's disbursement and reporting system. When we asked for a list of CPD-funded assets, the field offices stated that we would need to obtain the information from the grantees. They stated that HUD regulations did not require field offices to maintain such a list. However, when a situation occurs in which CPD funds a project and program objectives are at stake, CPD should have taken the initiative to establish and implement specific formal policies and procedures for the field offices and grantees to follow to ensure assets were protected and program objectives were met. As part of the formal policies and procedures, CPD could have requested lists from the grantees to show what funds and projects were managed by the defunct redevelopment agencies. If CPD had taken these proactive measures, it would have provided field offices with additional information to assist in the monitoring of grantees' CPD-funded projects impacted by the State's mandated closure of redevelopment agencies.
- Comment 3** We appreciate CPD's efforts to conduct reviews of grantees such as the Cities of San Jose, San Francisco, and Los Angeles during fiscal year 2014. However, it should be noted that our report results prompted CPD to conduct reviews of the grantees in question.

- Comment 4** We understand that the State, not CPD, was the responsible party that initiated the dissolution of the redevelopment agencies. We also understand that CPD held discussions with the State to discuss the situation and the roles of the redevelopment agencies to the grantees. However, CPD should have established formal policies and procedures for the grantees and field offices to ensure that assets were protected and used to meet program objectives.
- Comment 5** We agree that 24 CFR 85.31 was incorrectly cited throughout the report, as it is not listed as one of the applicable uniform administrative requirements in 24 CFR 570.502. We have removed this regulation from the report. For clarification, 24 CFR 570.505 only appeared on pages 7 and 8 of the report. The applicable regulation should have been 24 CFR 570.705, as it relates to loan requirements that the grantee and subrecipients must adhere to within the executed agreements. 24 CFR 570.503 is applicable to the review as it provides information to required elements within the executed agreements between the grantee and subrecipient. We corrected the referenced regulation on pages 6 and 8 of the report.
- Comment 6** We acknowledge there are no current HUD regulations requiring CPD to monitor the transfer of CPD-funded assets. We agree that the grantees are responsible for monitoring the subrecipients. However, CPD, as the awarding agency is responsible for ensuring that the grantees can meet the specified program objectives. During the State's mandate to close redevelopment agencies, or subrecipients to the grantees, CPD should have taken the necessary actions to provide field offices and grantees formal policies and procedures to ensure that the State's action did not affect grantees' ability to meet the program objectives. Without any formal policies and procedures, as well as lists of CPD-funded assets from the grantees, CPD may not be able to ensure that grantees can accomplish program objectives with minimal impact from the State's actions.
- Comment 7** We requested agreements between the grantees and the redevelopment agencies, also known as subrecipients, but some were missing. Of the agreements provided to us, some were unsigned or incomplete. In most instances, the grantees were unable to provide us executed agreements. Other grantees acknowledged issues with the agreements and were in the process of correcting those deficiencies. However, the agreements provided to us did not provide clear language related to reversion of assets. Since the redevelopment agencies are no longer active, the concern this audit raised is whether ownership rights and controls, as well as the executed agreements are still valid and applicable to the grantee.
- Comment 8** We requested all executed agreements including those with for-profit businesses, from the grantees to determine established ownership or legal claim to the CPD assets. Some of the agreements between the grantees and redevelopment agencies were missing. Of the agreements provided to us, some were unsigned or incomplete. For those agreements provided to us for review, we could not identify clear language related to the reversion of assets. Since the redevelopment agencies are no longer active, the concern this audit raised is whether ownership

rights and controls, as well as the executed agreements are still valid and applicable to the grantee and for-profit businesses.

- Comment 9** We are aware of the previous external reviews of the grantees administration and monitoring of CPD funds used at the Goodyear Tract, Blossom Plaza, Slauson Central and Avalon, Westlake Theatre, and Marlton Square. However, we conducted this internal review to determine whether CPD monitored the grantees' CPD-funded assets affected by the State-mandated shutdown of grantees' redevelopment agencies.
- Comment 10** In July 2013, the City of Los Angeles confirmed that it would include the Crenshaw Gateway property in its Long Range Property Management Plan as required by the State's redevelopment statutes. In its submittal, the City stated it will request that the designated local authority, the oversight board, and the State Department of Finance approve the transfer of this property to the City for continuation of its redevelopment activities. The City did not provide us documentation to corroborate CPD's statement that the submittal to the State occurred in January 2012.
- Comment 11** We are open to reviewing documents that would show that CPD ensured that grantees' executed agreements and other documents meet applicable HUD regulations including 24 CFR 570.705 during the audit resolution process. It should be noted that the results of our review factored into CPD scheduled reviews of the Cities of San Jose and San Francisco.
- Comment 12** Our audit period, covering January 1, 2011, to December 31, 2012, allowed us to obtain background information about the State's action to dissolve the redevelopments and its potential effect on grantees' ability to meet CPD program objectives. This background information predated the February 1, 2012 deadline established by the State. Further, we understand that the State's mandate is an ongoing process and the State's actions are not yet concluded.
- Comment 13** The report accurately stated that only 20 projects from three grantees with the highest funded assets were selected as part of the review. Based on the sampled results, there is the potential that more CPD-funded assets managed by defunct redevelopment agencies could have the same issues if CPD does not implement our recommendations.

Appendix C

LISTING OF SAMPLED CPD-FUNDED ASSETS

City of San Francisco:

Bayview Hunters Point

Status: Completed and occupied
Type of funding: CDBG



YBC – Marriott

Status: Completed and occupied
Type of funding: CDBG



YBC – Metreon

Status: Completed and occupied
Type of funding: CDBG



YBC – Howard Street

Status: Completed and occupied
Type of funding: CDBG



City of San Jose:

Masson: 161 W. Santa Clara Street

Status: Completed and occupied
Type of funding: Section 108



Security: 84 S. First Street

Status: Completed and occupied
Type of funding: Section 108



EU: 35 & 49 E. Santa Clara Street

Status: Completed and occupied
Type of funding: Section 108



City of Los Angeles:

Marlton Square

Status: Undeveloped vacant lot
Type of funding: Section 108, BEDI, EDI, and CDBG



Noho Commons Project

Status: Completed and occupied
Type of funding: Section 108 and BEDI



Slauson Central Shopping Center

Status: Site under construction
Type of funding: Section 108 and EDI



Goodyear Tract Brownfields Demonstration Site

Status: Under construction
Type of funding: Section 108 and BEDI



Goodyear Tract Land Acquisition

Status: Vacant building
Type of funding: CDBG



Crenshaw Gateway

Status: Undeveloped vacant lots
Type of funding: CDBG



Blossom Plaza

Status: Vacant building and lot
Type of funding: CDBG



Westlake Theatre

Status: Building (unknown if occupied)
Type of funding: CDBG



Appendix D

CRITERIA

24 CFR 85.42, Retention and access requirements for records.

- (a) Applicability.
 - (1) This section applies to all financial and programmatic records, supporting documents, statistical records, and other records of grantees or subgrantees which are:
 - (i) Required to be maintained by the terms of this part, program regulations or the grant agreement, or
 - (ii) Otherwise reasonably considered as pertinent to program regulations or the grant agreement.
- (c) Starting date of retention period
 - (2) Real property and equipment records. The retention period for real property and equipment records starts from the date of the disposition or replacement or transfer at the direction of the awarding agency.
 - (3) Records for income transactions after grant or subgrant support. In some cases grantees must report income after the period of grant support. Where there is such a requirement, the retention period for the records pertaining to the earning of the income starts from the end of the grantee's fiscal year in which the income is earned.

24 CFR 570.503, Agreements with subrecipients.

- (b) At a minimum, the written agreement with the subrecipient shall include provisions concerning the following items:
 - (2) *Records and reports.* The recipient shall specify in the agreement the particular records the subrecipient must maintain and the particular reports the subrecipient must submit in order to assist the recipient in meeting its recordkeeping and reporting requirements.
 - (7) *Reversion of assets.* The agreement shall specify that upon its expiration the subrecipient shall transfer to the recipient any CDBG funds on hand at the time of expiration and any accounts receivable attributable to the use of CDBG funds. It shall also include provisions designed to ensure that any real property under the subrecipient's control that was acquired or improved in whole or in part with CDBG funds (including CDBG funds provided to the subrecipient in the form of a loan) in excess of \$25,000 is either:
 - (i) Used to meet one of the national objectives in §570.208 (formerly § 570.901) until five years after expiration of the agreement, or for such longer period of time as determined to be appropriate by the recipient; or
 - (ii) Not used in accordance with paragraph (b)(7)(i) of this section, in which event the subrecipient shall pay to the recipient an amount equal to the current market value of the property less any portion of the value attributable to expenditures of non-CDBG funds for the acquisition of, or improvement to, the property. The payment is program income to the recipient. (No payment is required after the period of time specified in paragraph (b)(7)(i) of this section.)

24 CFR 570.506, Records to be maintained.

Each recipient shall establish and maintain sufficient records to enable the [HUD] Secretary to determine whether the recipient has met the requirements of this part. At a minimum, the following records are needed:

- (d) Records which demonstrate compliance with §570.505 regarding any change of use of real property acquired or improved with CDBG assistance.

570.705 Loan requirements.

- (b) *Security requirements.* To assure the repayment of debt obligations and the charges incurred under paragraph (g) of this section and as a condition for receiving loan guarantee assistance, the public entity (and State and designated public agency, as applicable) shall:
 - (1) Enter into a contract for loan guarantee assistance with HUD, in a form acceptable to HUD, including provisions for repayment of debt obligations guaranteed hereunder;
 - (2) Pledge all grants made or for which the public entity or State may become eligible under this part; and
 - (3) Furnish, at the discretion of HUD, such other security as may be deemed appropriate by HUD in making such guarantees. Other security shall be required for all loans with repayment periods of ten years or longer. Such other security shall be specified in the contract entered into pursuant to § 570.705(b)(1). Examples of other security HUD may require are:
 - (i) Program income as defined in § 570.500(a);
 - (ii) Liens on real and personal property;
 - (iii) Debt service reserves; and
 - (iv) Increments in local tax receipts generated by activities carried out with the guaranteed loan funds.

Title 42 USC Sec. 5308 of the Housing and Community Development Act of 1974, Guarantee and commitment to guarantee loans for acquisition of property.

d. Repayment contract; security; pledge by State

To assure the repayment of notes or other obligations and charges incurred under this section and as a condition for receiving such guarantees, the [HUD] Secretary shall require the issuer to-- enter into a contract, in a form acceptable to the Secretary, for repayment of notes or other obligations guaranteed hereunder; pledge any grant for which the issuer may become eligible under this chapter; and furnish, at the discretion of the Secretary, such other security as may be deemed appropriate by the Secretary in making such guarantees, including increments in local tax receipts generated by the activities assisted under this chapter or dispositions proceeds from the sale of land or rehabilitated property.