OFFICE OF AUDIT
REGION 2
NEW YORK, NEW JERSEY

The City of Elmira, New York

Community Development Block Grant Program

2014-NY-1004 MAY 20, 2014

Issue Date: May 20, 2014

Audit Report Number: 2014-NY-1004

TO: William O'Connell,
Director, Community Planning and Development, Buffalo, NY, 2CD

//SIGNED//Joseph Vizer
for
FROM: Edgar Moore,
Regional Inspector General for Audit, New York-New Jersey Region, 2AGA

SUBJECT: The City of Elmira, NY, Did Not Always Administer Its CDBG Program in Accordance With HUD Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our audit of the City of Elmira, NY's Community Development Block Grant program.

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 (212) 264-4174.

May 20, 2014

The City of Elmira, NY, Did Not Always Administer Its CDBG Program in Accordance With HUD Requirements

Highlights

Audit Report 2014-NY-1004

What We Audited and Why

We audited the City of Elmira, NY's administration of its Community Development Block Grant (CDBG) program based on our risk analysis and funding received by the City. The objectives of the audit were to determine whether the City (1) ensured that program activities were adequately documented and administered in accordance with U.S. Department of Housing and Urban Development (HUD) regulations, and (2) expended CDBG funds for eligible activities.

What We Recommend

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development instruct the City to (1) provide documentation regarding $200,000 in unsupported costs so that HUD can determine the eligibility of the costs; (2) repay $25,062 in ineligible costs; (3) provide supporting documentation for rehabilitation program delivery costs; and (4) establish and implement controls to ensure compliance with program requirements, that costs are charged to the benefiting programs, and that assets are properly safeguarded and duties are properly segregated.

What We Found

City officials did not always (1) ensure that program activities were adequately documented and administered in accordance with HUD regulations, and (2) expend CDBG funds for eligible activities. Specifically, the City charged costs to its CDBG program without adequate documentation to show that the costs met a national objective or benefited the CDBG program. In addition, excessive administrative program delivery costs were charged to the CDBG program, including costs for administering a State program. We also noted deficiencies in the City's ability to safeguard assets and segregate duties. These deficiencies occurred because City officials had not placed adequate emphasis on establishing and implementing the needed controls to ensure compliance with program requirements, including documenting compliance with national objectives, properly allocating costs to the programs receiving the benefit, and safeguarding assets and segregating duties.

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BACKGROUND AND OBJECTIVES

The Community Development Block Grant (CDBG) Entitlement Communities Grants program is authorized under Title 1 of the Housing and Community Development Act of 1974, Public Law 93-383, as amended (42 U.S.C. (United States Code) 5301 et seq.), and provides annual grants on a formula basis to entitled cities and counties 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.

Entitlement communities develop their own programs and funding priorities. However, grantees must give maximum feasible priority to activities that benefit low- and moderate-income persons. A grantee may also carry out activities that aid in the prevention or elimination of slums or blight. Additionally, grantees may fund activities when the grantee certifies that the activities meet other community development needs having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community and other financial resources are not available to meet such needs. CDBG funds may not be used for activities that do not meet these broad national objectives.

According to the U.S. Department of Housing and Urban Development's (HUD) Integrated Disbursement and Information System,[1] for fiscal years 2010 through 2012, the City of Elmira, NY, was awarded $3.74 million in CDBG funds, which was allocated to 21 activities in 2010, 24 activities in 2011, and 14 activities in 2012.

The City operates under a mayor-city manager-council form of government, and its CDBG activities are administered both in-house, through the City's Department of Community Development, and by subrecipient organizations. The City is responsible for overseeing, monitoring, and managing CDBG activities. The files and records related to the City's CDBG program are maintained at City Hall, Third Floor, 317 East Church Street, Elmira, NY.

The objectives of the audit were to determine whether the City (1) ensured that program activities were adequately documented and administered in accordance with HUD regulations and (2) expended CDBG funds for eligible activities.

[1] The Integrated Disbursement and Information System is a nationwide drawdown and reporting system for HUD's four community planning and development grant programs: the CDBG, HOME Investment Partnerships, Emergency Shelter Grants, and Housing Opportunities for Persons With AIDS programs. The system allows grantees to request their grant funding from HUD and report on their program accomplishments. HUD uses these data to report to Congress and monitor grantees.

RESULTS OF AUDIT

Finding: City Officials Did Not Always Administer the CDBG Program in Accordance With HUD Requirements

City officials did not always (1) ensure that program activities were adequately documented and administered in accordance with HUD regulations, and (2) expend CDBG funds for eligible activities. Specifically, they charged costs to the City's CDBG program without adequate documentation to show that the costs met a national objective or benefited the CDBG program. In addition, excessive administrative program delivery costs were charged to the CDBG program, including costs for administering a State program. We also noted deficiencies in the City's ability to safeguard assets and segregate duties. These deficiencies occurred because City officials had not placed adequate emphasis on establishing and implementing the controls needed to ensure compliance with program requirements, including documenting compliance with national objectives, properly allocating costs to the programs receiving the benefit, and implementing other needed controls to properly safeguard assets and segregate duties. As a result, unsupported costs of $797,048 and ineligible costs of $25,062 were expended for activities that did not benefit the City's CDBG program, including additional charges for State rehabilitation program delivery costs, and other assets were at risk of being misappropriated.

City Files Did Not Always Contain Adequate Documentation

City files did not always contain documentation to support whether the costs incurred met a national objective or benefited the CDBG program. As a result, $225,062 in costs charged to the CDBG program was either unsupported or ineligible. Specifically, a $200,000 commercial loan was considered to be unsupported, and $18,027 paid to a nonprofit for its administrative costs and $7,035 paid to an architecture firm for work related to a State grant were ineligible since these costs were not adequately supported with documentation to show that the costs benefited the CDBG program or met a national objective. The details are described below:

$200,000 Commercial Loan Did Not Meet a National Objective

The City, through its subrecipient, Southern Tier Economic Growth, administers its CDBG revolving Economic Development Loan programs, including a commercial loan program and an industrial loan program. A commercial loan of $200,000 was made on April 19, 2011, at a 2 percent interest rate to relocate several manufacturing businesses into one central location. As of September 30, 2013, the loan was current with an unpaid principal balance of $136,416, but it had not led to the creation of any jobs. Regulations require that funds used for public benefit create or retain at least one full-time-equivalent, permanent job per $35,000 in CDBG funds used, which would have required the creation or retention of at least six full-time jobs.[2] However, the project eligibility form for the loan required that the subrecipient create 14 full-time jobs, with 8 to be filled by low- to moderate-income persons. According to loan documents and the subrecipient's procedures, the borrower had 3 years to create the jobs. However, since the loan was made on April 19, 2011, the borrower had only until April 19, 2014, to create the 14 jobs, or it would not meet a national objective of the program.

In addition, there was a potential conflict of interest as the loan was made to a local for-profit corporation, the president of which was also on the board of directors of the subrecipient that made and administered the loan on behalf of the City. The corporation's president was not on the subrecipient's loan committee but was a member of its board of directors. HUD regulations prohibit participation in the administration of a contract if there is a real or apparent conflict of interest.[3]

Since no jobs had been created to evidence meeting a national objective of the program, there was a potential conflict of interest, and no related parties' waiver had been requested from or provided by HUD related to the apparent conflict of interest, we considered the use of CDBG program funds to provide the loan to be unsupported.

$18,027 Paid to a Subrecipient Did Not Benefit the CDBG Program

The City's subrecipient, which administers its CDBG-funded revolving Economic Development Loan program, created a sister corporation, Southern Tier Economic Development Corporation. This nonprofit corporation was established to be the owner of a downtown arena facility that was constructed in part with a $4 million Section 108 loan. The Elmira Downtown Arena, LLC, was to manage and operate the arena. Our review revealed that several invoices for the nonprofit corporation had been paid with CDBG funds, although these costs did not benefit the CDBG program. The City's attorney explained that over the years, the City had paid various administrative costs for the nonprofit for legal and accounting fees and liability insurance. The City's attorney indicated that these costs were always paid from the City's general funds because they were considered to be City expenses.

[2] Regulations at 24 CFR (Code of Federal Regulations) 570.209(b) provide the standard for evaluating public benefit and that the grantee is responsible for ensuring that at least the minimum required public benefit is obtained from expending CDBG funds.

[3] Regulations at 24 CFR 85.36(b)(3) require that the grantee and subgrantee maintain standards of conduct, which prohibit participation in the selection, award, or administration of a contract involving Federal funds if there is a real or apparent conflict of interest.

We tested all 10 of the transactions paid on behalf of the nonprofit with CDBG funds since 2009, which totaled $18,027. These costs included payments for income tax return preparation and liability insurance with no apparent benefit to the CDBG program or evidence of meeting a national objective. Therefore, we considered these costs to be ineligible.

$7,035 Paid to an Architecture Company Did Not Benefit the CDBG Program

Five payments totaling $7,035 were made to an architecture company relating to a State grant to complete a National Register Historic District nomination for the Maple Brand Park Area.[4] CDBG funds were used because funds had not been received from the State of New York. The director of the City's Department of Community Development indicated that the CDBG administration line item would be reimbursed for the $7,035 in costs incurred when State funding was received. The practice of using CDBG funds to prepay costs relating to another funding source is a control weakness in the safeguarding of CDBG assets, and it should be prohibited. In this instance, the costs were incurred relating to a State grant with no bearing on the CDBG program, and, therefore, the costs would be ineligible at the time they were incurred.[5] Further, on September 11, 2013, the community development finance director confirmed that a "due from State Grants" receivable had not been established on the CDBG books relating to the prepaid expenses. The lack of a control asset due from account increased the possibility that the funds might not be repaid to the CDBG program.[6]

After our review and before preparation of the draft report, the Department of Community Development director informed us that the State grant funding had been received and the CDBG program had been reimbursed for these costs. However, we considered this to be a significant weakness as CDBG funds were not properly safeguarded and the accounting treatment was not acceptable.

[4] The National Register of Historic Places is the official list of the Nation's historic places worthy of preservation, authorized by the National Historic Preservation Act of 1966. The National Park Service's National Register of Historic Places is part of a national program to coordinate and support public and private efforts to identify, evaluate, and protect America's historic and archeological resources.

[5] Regulations at 24 CFR 570.200(a), Determination of eligibility, provide that for costs to be eligible, they must meet a national objective and benefit the CDBG program and costs incurred must be allocated in accordance with Federal cost principles, which require the costs to be necessary and reasonable and properly allocable to the CDBG program.

[6] Regulations at 24 CFR 85.20, Standard for financial management systems, (b), provides that grantees and subgrantees must maintain records, which adequately identify the source and application of funds provided for financially assisted activities and that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and ensure that it is used solely for authorized purposes.

Costs of Administering the Homeowner Rehabilitation Program Were Not Reasonable

The City administers a CDBG homeowner rehabilitation activity and also charges the CDBG program for the rehabilitation administration costs (program delivery costs) related to this program. The homeowner rehabilitation costs consist of loans and grants to homeowners for various rehabilitation work, while the program delivery costs should primarily be for the salary and fringe benefit costs of a housing inspector and a housing rehabilitation assistant. From July 2010 through June 2011 $230,000 was charged to the CDBG program for rehabilitation program delivery. We tested 10 biweekly payrolls during that period and determined that the payroll charges were adequately supported. However, we noted that the total charges for program delivery costs were not reasonable, economical, or efficient in proportion to the level of actual rehabilitation costs for work completed at homeowner residences. For instance, the actual cost of homeowner rehabilitation for the past 5 program years and as of June 27, 2013, was $527,096, while the program delivery cost was $865,287 for a total of $1,392,383. Therefore, the program delivery costs represented 164 percent of the actual homeowner rehabilitation costs.

The City also received funding from the State to run a State-funded rehabilitation program. However, the director of the Community Development Department informed us that since the State did not provide administrative funds as part of its grants, the Department charged employee costs to the CDBG rehabilitation program delivery activity for the State-funded activities as well as the CDBG-funded activities. Thus, the City had been carrying out State-funded activities with CDBG funds and then classifying those costs as program delivery costs related to CDBG-funded rehabilitation activities.

Using unaudited data provided to us for the period 2008 through 2012, we estimated that the City expended more than $1.7 million on actual rehabilitation costs, consisting of 31 percent for the CDBG rehabilitation program and 69 percent for the State rehabilitation program (see chart below).

Total CDBG and State direct rehabilitation expenditures

Year	CDBG rehabilitation expenditures	State rehabilitation expenditures	Total expenditures without program delivery costs
2008	$76,865	$162,595	$239,460
2009	170,655	278,225	448,880
2010	137,933	234,874	372,807
2011	128,315	258,714	387,029
2012	13,328	240,000	253,328
Total	$527,096	$1,174,408	$1,701,504
Percentage of total	31%	69%	100%

During the same period, the City charged the CDBG program a total of $865,287 for program delivery (rehabilitation administrative) costs, which included the costs of administering the State rehabilitation program. As a result, the CDBG program absorbed all of the administrative costs of the State rehabilitation program. If the program delivery administrative costs were allocated in proportion to the total estimated expenditures of the CDBG and State rehabilitation programs, the State should have paid approximately 69 percent of the total program delivery costs, which would have been $597,048 ($865,287 x 69%). Further, we estimated the average annual amount of program delivery costs that should have been paid by the State program to be approximately $119,410 ($597,048 / 5 years). Federal cost principles require that for costs to be allowable, they must be reasonable and allocable to the Federal program being charged.[7] While there are a number of acceptable methods by which the City could have estimated these costs, including direct time spent on the State and CDBG rehabilitation activities, which may have resulted in different amounts, we considered the estimated costs that could have been allocated to the State program ($597,048) to be unsupported.

There Were Control Weaknesses Related to Safeguarding Assets and Segregation of Duties

Interviews with City officials and a review of program and financial files identified control weaknesses related to the safeguarding of assets and segregation of duties; specifically,

[7] Regulations at 2 CFR Part 225, Appendix A - General Principles for Determining Allowable Costs, Section C - Basic Guidelines, subsection 2, requires that for costs to be allowable, they must be reasonable. Subsection 3(a) provides that for costs to be allocable to a Federal program, they must be in accordance with the relative benefits received.

- The Department of Community Development had a chart of accounts but lacked specific written procedures covering the CDBG accounting system.

- CDBG journal entries were not always fully explained, nor were the entries formally approved by the community development director. To enhance controls, the City should maintain a general journal that provides written explanations documenting the reason(s) and methodology for the entries, and all entries should be formally approved by the community development director.

- The finance director, who was responsible for cash receipts, reconciled the bank statements but did not sign checks. To enhance controls, the Department of Community Development should consider assigning the function of bank reconciliations to an employee who is not responsible for cash receipts.

- The Department of Community Development did not use purchase orders for all items acquired. This practice was contrary to City policy and was a safeguarding of assets control weakness. To enhance controls, the Department should follow City purchasing procedures.

- The Department of Community Development did not document the receipt of all purchased items. This was a safeguarding of assets control weakness. To enhance controls, the Department should document the receipt of all purchased items (for example, by preparing receiving reports).

- All CDBG-related mail, including vendor invoices, was opened by the finance director. An employee who is not involved with the accounting function should open the mail and keep a log of all received mail.

Regulations at 24 CFR (Code of Federal Regulations) 85.20(b)(3) provide that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and ensure that it is used solely for authorized purposes. If City officials enhance the above controls, they can work toward achieving this goal.

Conclusion

City officials did not always (1) ensure that program activities were adequately documented and administered in accordance HUD regulations and (2) expend CDBG funds for eligible activities. These deficiencies occurred because City officials did not place adequate emphasis on establishing and implementing the controls needed to ensure compliance with program requirements, including documenting compliance with national objectives, properly allocating costs to the programs receiving the benefit, and implementing other needed controls to properly safeguard assets. As a result, unsupported costs of $797,048 (200,000 + 597,048) and ineligible costs of $25,062 were expended with CDBG funds for activities that did not benefit the City's CDBG program, including estimated charges for State rehabilitation program delivery costs, and other assets were at risk of misappropriation.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development instruct City officials to

1A. Submit documentation to justify the unsupported costs of $200,000 incurred for an economic development loan so that HUD can make an eligibility determination. For any costs determined to be ineligible, HUD should require the City to reimburse the CDBG program from non-Federal funds.

1B. Require the subrecipient to request a waiver related to the apparent conflict of interest and implement standards of conduct procedures that prohibit participation in the selection, award, or administration of a contract involving Federal funds if there is a real or apparent conflict of interest.

1C. Repay from non-Federal funds the ineligible costs of $18,027 that were paid to a subrecipeint, which did not benefit the CDBG program.

1D. Provide documentation regarding the repayment of the $7,035 that was paid an architecture firm related to a State grant to ensure that it was properly repaid to the CDBG program from non-Federal funds.

1E. Establish controls to ensure that grant- and subgrant-supported activities are adequately monitored and administered to provide assurance that funds have been used only for eligible activities, costs incurred are necessary and reasonable, and national objectives have been attained.

1F. Establish controls to ensure that CDBG funds are not used to pay for costs related to other funding sources or programs.

1G. Provide documentation to support the reasonableness and eligibility of the administrative program delivery costs charged to the CDBG program, including $597,048 in program delivery costs that could have been allocated to the State program, and repay the CDBG program from non-Federal funds any amounts determined to be unreasonable or ineligible.

1H. Establish procedures to ensure that the costs of administering the State-funded rehabilitation program are no longer charged to the CDBG program.

1I. Establish controls to ensure that assets are adequately safeguarded and duties are adequately segregated.

SCOPE AND METHODOLOGY

We performed our onsite work at the City's offices between August and November 2013. The audit scope covered the period July 2011 through June 2013 and was extended as necessary.

To accomplish our audit objectives, we

- Reviewed applicable HUD regulations, the Code of Federal Regulations, and other requirements and directives that govern the CDBG program.
- Reviewed the City's applicable policies and procedures used to administer CDBG activities.
- Reviewed subrecipient activities to determine whether national objectives were met.
- Interviewed City officials responsible for administering the City's CDBG program.
- Obtained and reviewed program and financial documentation from the City and its subrecipients pertaining to the CDBG activities reviewed.
- Reviewed HUD's monitoring reports and files for the City's community planning and development programs.
- Reviewed independent public accountant audits and financial reporting.
- Reviewed costs charged to the CDBG program for activities tested during the review, along with the applicable supporting documentation provided.
- Reviewed data from HUD's Integrated Disbursement and Information System for background and informational purposes. We relied in part on computer-processed data for obtaining background information on the City's expenditure of CDBG funds. We performed a minimal level of testing and found the data to be adequate for our purposes.

For fiscal years 2010 through 2012, the City was awarded $3.74 million in CDBG funds, and those funds were allocated to 21 activities in 2010, 24 activities in 2011, and 14 activities in 2012.

We reviewed internal controls and five of the City's CDBG activities. Selection of the activities reviewed focused primarily on higher funded activities and also included subrecipient-administered activities.

The City, through its subrecipient, Southern Tier Economic Growth, administers CDBG revolving Economic Development Loan programs, including a commercial loan program and an industrial loan program. As of June 2013, there were 12 active loans made between August 2006 and February 2013 totaling $755,000. Since 2010, the subrecipient has made a total of six loans. Two of the loans were industrial loans, and the remaining four loans were commercial loans. We selected two industrial loans and one commercial loan for review.

Activities were not selected using statistical sampling methodologies, and the results of the sampling are applicable only to the activites tested, and no projection of the results of the audit testing was made to the activities that were not selected for testing.

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 objectives.

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 operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

- Reliability of financial reporting – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

- Compliance with applicable laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.

- Safeguarding of resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

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 the effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

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

- City officials did not have adequate controls over the efficiency and effectiveness of program operations when they did not establish adequate administrative controls to ensure that CDBG funds were not used to fund a nonprofit's operating costs that did not benefit the CDBG program or meet a national objective (see finding).

- City officials did not have adequate controls over compliance with laws and regulations when they did not address or seek a HUD waiver relating to a potential conflict of interest associated with a CDBG-funded economic development loan, which also had not met a national objective of the program at the time of the review (see finding).

- City officials did not have an adequate system to ensure that resources were properly safeguarded when they did not ensure that CDBG funds were not used to pay for costs associated with other funding sources. In addition, duties were not always optimally segregated, procedures covering the CDBG accounting system were not documented, journal entries were not formally approved by the community development director, purchase orders were not always used for items acquired, and receiving reports were not always prepared to document the receipt of all purchases, which diminished the City's controls over the safeguarding of resources (see finding).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/	Unsupported 2/
1A		$200,000
1C	$18,027	
1D	7,035	
1G		597,048
Total	$25,062	$797,048

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 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**

CITY OF ELMIRA NEW YORK

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April 30, 2014

Mr. Edgar Moore
Regional Inspector General for Audit
U.S Department of Housing and Urban Development
Office of Inspector General
26 Federal Plaza, Room 3430
New York, NY 10278-0068

Dear Mr. Moore:

Please find below the City of Elmira's comments regarding the Draft Audit Report provided to the City of Elmira on April 21, 2014 on the recently completed audit of the City of Elmira Community Development Block Grant Program.

$200,000 Commercial Loan Did Not Meet a National Objective

Comment 1

Job creation: The $200,000 loan was part of a $2.2 million project with the goal of relocating various manufacturing businesses (and 45 +/- jobs) from outside of the City into a central city location to grow the companies. This loan activated a vacant 30,000 sq. ft. space and it is being actively marketed for additional business tenants. At the time of the loan closing, all economic news and indication was that the "Great Recession" had ended, however the Southern Tier, and in particular Elmira, has not witnessed any relief. Over the past year, the Elmira MSA lost 1,300 private sector jobs, second only to Binghamton in job loss in New York State, a 4.5% decline. The Director of Community Development and the President of Southern Tier Economic Growth met with the company in April 2014 to discuss job creation and during the course of this discussion, the President felt that there was a significant chance that jobs would be created but that meeting the low-mod job creation requirements has proven to be difficult. The company is willing to seek alternative financing and repay the CDBG loan principal off which the City and STEG will pursue with them with the goal of having this accomplished by June 30, 2014.

Comment 2

Conflict of Interest: Southern Tier Economic Growth's (STEG) Board of Directors comprises 70 business and community leaders including the City Manager and the majority of the City of Elmira's manufacturers have a representative on the Board of Directors. The President of the Corporation served by the loan does not serve as an officer of STEG nor on any of STEG's committees, including the Loan Review Committee as noted in the Draft Audit Report. The City and STEG will request a waiver from HUD on the basis that the President of the Corporation

Ref to OIG Evaluation **Auditee Comments**

served was not involved in the decision-making process if the company does not repay the remaining principal of the CDBG loan in its entirety. Going forward, the City and STEG will not extend a loan funded with HUD funds without first identifying if there are any real or apparent conflicts of interest, If any are identified, requesting HUD review any apparent conflicts of interests for a waiver and real conflicts will be denied.

$18,027 Paid to a Subrecipient Did Not Benefit the CDBG Program

Comment 3

The City of Elmira does not dispute that these costs are ineligible because they did not benefit the CDBG program and should be re-paid with non-federal funds.

$7,035 Paid to an Architecture Company Did Not Benefit the CDBG Program

Comment 4

The City acknowledges that payments paid to an architecture firm to complete a National Register Historic District nomination is a control weakness and in the future CDBG funds will not be utilized to pre-pay other grant expenses and the necessary controls will be put into place. State funds were received on December 5, 2013 and deposited into the City's CDBG account and an entry was made in Quickbooks to reimburse the CDBG administration line. The preparation of this nomination was charged as an administrative/planning expense meant to spur revitalization of a neighborhood and the preservation of historic properties which is a Consolidated Plan priority.

Costs of Administering the Homeowner Rehabilitation Program Were Not Reasonable

Comment 5

In reference to the administrative program delivery costs charged to the CDBG program for the administration of the state-funded housing rehabilitation program, the City would just like to reiterate that in the past municipalities were ineligible to receive funds from the state to cover administrative costs. Under the state program only Neighborhood Preservation Companies (NPC)/Rural Preservation Companies (RPC) were allowed to charge for administration, however in the 2013-2014 state Request for Proposals, non-NPC grantees were eligible to receive up to a ten percent (10%) administrative allowance which will be pursued by the City in the future to offset CDBG program delivery costs. Please note that the City of Elmira did not apply for funding under the 2013-2014 because of remaining funds awarded under the 2012 funding round. The City of Elmira has utilized state housing rehabilitation funds to match or leverage CDBG funds a midst decreasing CDBG program entitlement awards in order to continue to assist low income homeowners address an aging housing stock. Further, the City has included the use of these state funds for housing rehabilitation in its Annual Action Plans and CAPER Reports submitted to HUD. The HUD Buffalo Field Office in its Program Year Report for the City of Elmira covering July 1, 2012- June 30, 2013, stated, " Per unit costs were not excessive and CDBG program delivery expenses were reasonable (page 4)." The City of Elmira will continue to make efforts to control program delivery costs and in the future will apply for the maximum administrative allowance allowed under the state program. The City would like to note that the state rehabilitation expenditure information requested from the City and utilized for the chart entitled Total CDBG and State direct rehabilitation expenditures was for calendar year and the information utilized for the CDBG rehabilitation expenditures column was based on program

Ref to OIG Evaluation | **Auditee Comments**

years. The CDBG expenditure information was obtained from the City's IDIS PR-02 reports. Also, during the time period surveyed, there were rehabilitation activities set up in HUD's IDIS system that were categorized under the program year from which the funds originated (a prior year) despite the fact that they were expended in a subsequent year. Based upon the City's analysis and CDBG expenditures tracked in QuickBooks from July 1, 2008- June 30, 2013 were $1,019,921 and for that same period State rehabilitation expenditures were $1,040,071 for a total of $2,059,993 spent on low to moderate income housing rehabilitation within the City of Elmira. In other words, 49.5% of the total rehabilitation expenditures were CDBG related and 50.5% were paid for with state grant funds.

There Were Control Weaknesses Related to Safeguarding Assets and Segregation of Duties

Comment 6

The City of Elmira will establish controls to ensure that assets are adequately safeguarded and duties are adequately segregated. During the period covered by the audit scope (July 2011- June 2013), the Department of Community Development underwent a transition resulting from the retirements of two staff members with 30+ years of experience in December 2011 and due to CDBG grant reductions, the Department had to reduce its staff by two following those retirements. The City of Elmira Chamberlain's Office has agreed to review all bank reconciliations completed by the Finance Director to enhance controls. The Department of Community Development is now ensuring that purchase orders are utilized for all purchased items and CDBG journal entries provide for written explanations that are formally approved by the Community Development Director.

If you have any questions concerning our comments, please do not hesitate to contact Jennifer Miller, Director of Community Development at (607) 737-5692 or jennmiller@cityofelmira.net.

Sincerely,

Susan J. Skidmore
Mayor

Cc: Jennifer Miller, Director of Community Development
Kimberlee Balok Middaugh, Esq., City Manager
John Zielinski, City Chamberlain

OIG Evaluation of Auditee Comments

Comment 1 City officials indicated that meeting the low-mod job creation requirement has proven to be difficult and that the company is willing to repay the CDBG loan. City officials indicated that they will pursue repayment of the $200,000 loan by June 30, 2014. The City officials' comments and planned actions are responsive to the finding and recommendation.

Comment 2 City officials stated that they would request a waiver from HUD on the prior potential conflict of interest. Also, City Officials and STEG will not extend any loan involving HUD funds without first identifying any real or apparent conflicts of interest and requesting a HUD review and waiver. The City officials' comments and planned actions are responsive to the finding and recommendations.

Comment 3 City officials agreed that the $18,027 paid to a subrecipeint was ineligible because it did not benefit the CDBG program and should be repaid with non-Federal funds. The City officials' comments and planned actions are responsive to the finding and recommendations.

Comment 4 City officials agreed that $7,035 paid to architecture firm for a non-CDBG historic district nomination was a control weakness and that CDBG funds will not be used to prepay expenses for other grants. City officials indicated that the $7,035 had been repaid to the CDBG program. The City officials' comments are responsive to the finding and recommendations, however, the HUD Buffalo Community Development staff should verify the accounting treatment related to the advance and repayment of the funds as part of the audit resolution process.

Comment 5 City officials indicated that in the past municipalities were not eligible to receive administrative costs from the state, but now the City can and will apply for funds to administer the State rehabilitation program. City officials indicated that the HUD Buffalo Office in its review of the CDBG program for the year ended June 30, 2013, stated that "Per unit costs and CDBG program delivery costs were reasonable." City officials also indicated that using actual expenditures from QuickBooks resulted in different results when comparing the amount of State rehabilitation expenditures to CDBG expenditures, and that rehabilitation expenditures applicable to State funding were only 49.5 percent compared to the 69 percent reported in OIG's chart in the report. City officials indicated that they will try to make efforts to control program delivery costs and apply for the maximum administrative allowance allowed by the State program. However, our review of the HUD report revealed that it did not clearly indicate that the reasonable program delivery costs were specifically applicable to the rehabilitation activity as opposed to the overall CDBG program. Furthermore, HUD program staff indicated that program delivery costs for the rehabilitation activity appeared high when we discussed the finding with them. The difference in the amounts and percentages of rehabilitation funded activities is based on what program and calendar years are included in the computation and can be attributed to timing differences. Therefore, City Officials should provide documentation to reconcile the differences in amounts expended per IDIS compared to the amounts expended per QuickBooks as part of the audit resolution process to support if the program delivery costs for the rehabilitation activity are reasonable. Note that although City officials' comments indicate that 50.5 percent of the total rehabilitation costs were applicable to the State program, all the program delivery and administrative costs were charged to the CDBG program, which does not appear to be proper as Federal cost principles require the costs to be reasonable and allocable to the program being charged.

Comment 6 City officials indicated that they will establish controls to ensure that assets are adequately safeguarded and duties are adequately segregated. Therefore, the City officials' comments and planned actions are responsive to the finding and recommendation.