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

FROM: *Edgar Moore*
Edgar Moore, Regional Inspector General for Audit, 2AGA

SUBJECT: The City of Buffalo Did Not Always Administer Its Community Development Block Grant Program in Accordance With HUD Requirements

HIGHLIGHTS

What We Audited and Why

We audited the City of Buffalo's (City) Community Development Block Grant (CDBG) program. We selected the City based on a hotline complaint, Hotline Case Number HL-09-0960, received on July 2, 2009. The complaint alleged that the City, the Buffalo Urban Renewal Agency, and the Buffalo Economic Renaissance Corporation misused CDBG funds. The complaint expressed concerns pertaining to 19 findings identified in the U.S. Department of Housing and Urban Development's (HUD) March 2009 monitoring report on the City's administration of its CDBG program. The objectives of the audit were to determine whether the City (1) administered its CDBG program effectively, efficiently, and economically in accordance with applicable rules and regulations, and (2) expended CDBG funds for eligible activities that met a national objective of the program.

What We Found

The City did not always follow applicable HUD regulations in its administration of the CDBG program. In addition, it did not always ensure that CDBG funds were expended for eligible activities that met a national objective of the program. Specifically, the City (1) disbursed CDBG program funds for questionable street

improvement expenditures, (2) did not adequately monitor its subrecipient-administered economic development program, and (3) charged ineligible and unsupported costs for clean and seal program activities to the CDBG program. As a result, program funds were used for ineligible and unsupported expenses and the City's ability to administer its CDBG program effectively and efficiently and ensure that the program's objectives were met was diminished. Consequently, the City is not able to demonstrate that it made the best use of CDBG funds to meet the community's needs.

What We Recommend

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development instruct the City to (1) reimburse from non-Federal funds \$467,429 for ineligible costs pertaining to street improvement projects not done and clean and seal code enforcement, (2) provide documentation to justify the more than \$22.8 million in unsupported costs for previously incurred general City maintenance expenses, transactions charged to the CDBG program income account, and unsupported clean and seal program costs, (3) reprogram the more than \$4.7 million in remaining economic development project funds if there is a lack of capacity, to ensure that these funds are put to better use for other eligible program activities, and (4) ensure that \$744,479 in fiscal year 2010 clean and seal program funds will be put to better use by developing administrative control procedures that will ensure compliance with CDBG program requirements. Any costs determined to be ineligible should be reimbursed from non-Federal funds.

Further, we recommend that the Director of HUD's Buffalo Office of Community Planning and Development require the City to suspend incurring costs and/or reimbursing itself for costs paid from the City's municipal general expense account for public facilities, economic development, and clean and seal activities until HUD determines that the City has the capacity to carry out these activities in compliance with HUD regulations.

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

Auditee's Response

We discussed the results of our review during the audit, provided a copy of the draft report to City officials, and requested their comments on February 17, 2011. We held an exit conference on March 8, 2011, and City officials provided their written comments on March 10, 2011, at which time they generally disagreed with the findings. The complete text of the auditee's response, excluding the exhibits, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Community Development Block Grant (CDBG) program was established by Title I of the Housing and Community Development Act of 1974, Public Law 93-383 as amended, 42 U.S.C. (United States Code) 5301. The program provides grants to State and local governments to aid in the development of viable urban communities. Governments are to use grant funds to provide decent housing and suitable living environments and to expand economic opportunities, principally for persons of low and moderate income. To be eligible for funding, every CDBG-funded activity must meet one of the program's three national objectives. Specifically, every activity, except for program administration and planning, must

- Benefit low- and moderate-income persons,
- Aid in preventing or eliminating slums or blight, or
- Address a need with a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare or the community.

The City of Buffalo, NY (City) is a CDBG entitlement grantee. The U.S. Department of Housing and Urban Development (HUD) awarded the City more than \$15.8 million in CDBG funding in fiscal year 2008, more than \$16 million in 2009, and more than \$17 million in 2010.¹ In addition, the City has received more than \$4.3 million in funds under the American Recovery and Reinvestment Act of 2009. These funds are available to support a variety of activities directed at improving the physical condition of neighborhoods by providing housing rehabilitation and public improvements and facilities, fostering economic development by providing technical and financial assistance to local businesses and creating employment, or improving services for low- and/or moderate-income households. The City operates under a mayor-council form of government, and its CDBG activities are administered both in-house, through the Buffalo Urban Renewal Agency (Agency) and the City's Office of Strategic Planning, and through outside nonprofit organizations like the Buffalo Economic Renaissance Corporation (Corporation). The City is responsible for overseeing, monitoring, and supporting the Corporation's CDBG activities. The files and records related to the City's CDBG program are maintained in City Hall, located in Buffalo, NY.

The objectives of the audit were to determine whether the City (1) administered its CDBG program effectively, efficiently, and economically in accordance with applicable rules and regulations, and (2) expended CDBG funds for eligible activities that met a national objective of the program.

¹ The City's CDBG fiscal year is May 1 through April 30.

RESULTS OF AUDIT

Finding 1: The City Charged Questionable Street Improvement Expenditures to Its CDBG Program

The City charged questionable street improvement expenditures to its CDBG program. Specifically, it used CDBG funds to reimburse its municipal general expense account for ineligible and unsupported City street improvement expenses, did not use CDBG funds to address the community's needs, and did not maintain sufficient procurement records. As a result, \$162,923 in ineligible costs and more than \$1.9 million in unsupported costs were charged to the program. Consequently, the City's ability to administer its CDBG program efficiently and effectively and ensure that CDBG program objectives were met was diminished. We attribute this deficiency to the City's unfamiliarity with HUD regulations, and its circumvention of the regulations and its own policies to expend CDBG funds quickly to prevent a reduction in future funding.

Ineligible and Unsupported Street Improvement Projects

On January 13, 2010, HUD notified the City that its line-of-credit ratio was 1.7 in comparison with its 2009 grant amount. To meet the 1.5 timeliness test for 2009, the City needed to draw down an additional \$3.3 million before March 2, 2010. Failure to meet this requirement would have resulted in a possible reduction in future funding by HUD. As a result, the City drew down just under \$3.3 million from the entitlement fund during February 2010. Specifically, on February 23, 2010, \$2.1 million was reimbursed to the City from CDBG funds for street improvement projects through 11 entitlement draws. We reviewed each of the 11 draws as part of our audit and determined that the drawdowns were for general City maintenance expenses that were incurred as early as June 2007.

Regulations at 24 CFR (Code of Federal Regulations) 570.200(a)(2) require the City to ensure and maintain evidence that each of its CDBG-funded activities meets one of the broad national objectives of the CDBG program. However, since the street improvement activities reviewed were not initially CDBG activities, the City did not maintain evidence from the time incurred 2007 through 2009 that the activities met a national objective and had a community benefit. In addition, work such as median and curb improvements and street-resurfacing projects were not performed on three different streets for which the City was reimbursed \$134,711. Also, the City received a duplicate reimbursement of \$28,212 in ineligible expenses for the resurfacing of a City street.

Further, for a number of the streets, we could not determine how the CDBG eligibility criteria were met. Although the City indicated that the work benefited low- to moderate-income residents in the area where the work was performed, some of the streets were in industrial or commercial business areas. As a result, we question the City's basis for determining the area served by certain street improvement projects, and recommend submission of information to support their service area determination. Federal requirements in 42 U.S.C. (United States Code) 5301(c) provide that to meet CDBG eligibility criteria, the work must principally benefit persons of low and moderate income. Further, since the remainder of the drawdowns reviewed was for previously incurred general City maintenance expenses that lacked monitoring documents to ensure compliance with national objectives, more than \$1.9 million is considered unsupported pending an eligibility determination by HUD. City officials expressed confusion in obtaining the proper paperwork from the Department of Public Works to support the corresponding vouchers.

Shown below are two pictures of public improvements on Academy Road that were not made.



The Agency reimbursed the City using CDBG funds for a median curb replacement project on Academy Road that was not done. The picture above illustrates that the median curb was not replaced.



Above is another picture of the Academy Road median, illustrating that the median curb was not replaced.

Shown below are two pictures of public improvements on West Parade Avenue between Best and East North Street that were not made.



The Agency reimbursed the City using CDBG funds for a street repaving project on West Parade Avenue that was not done. The picture above illustrates that the street was not repaved.



Above is another picture of West Parade Avenue, illustrating that the street was not repaved.

Improvement Projects Not Based on Community Needs

Contrary to CDBG regulations at 24 CFR Part 91, the City's public improvement projects were not based on the established goals and needs of the community based on the consolidated plan. The City is divided into nine area districts, each headed by a City council member. Rather than use CDBG funding based on the City's overall infrastructure needs, the City distributed the CDBG funds equally by the nine districts. For example, in fiscal year 2009, the City's Lovejoy District and Delaware District each were allocated \$57,778 for public improvements. However, the need for public improvements in the Lovejoy District may have been greater than that in the Delaware District. According to City officials, this distribution method was necessary to receive cooperation from the City's common council in approving the City's annual action plan. However, according to its own policies, the City's common council is to be advisory only and does not have the authority to dictate how CDBG funds are to be used by the City's Department of Public Works. As a result, it was questionable whether the public improvements expenditures reviewed were the most efficient and economical use of CDBG funds.

Shown below are three photographs of a Delaware District neighborhood benefiting from public improvements that were questionable based on community need.



The Agency reimbursed the City using CDBG funds for a curb and sidewalk replacement project on West Ferry Street, which was questionable based on community need. The picture above illustrates the neighborhood benefiting from the curb and sidewalk replacement project.



Above is another picture of the West Ferry Street neighborhood. The curb and sidewalk replacement project on this street was questionable based on community need.



Above is another picture of the West Ferry Street neighborhood. The curb and sidewalk replacement project on this street was questionable based on community need.

Procurement Records Not Maintained

Contrary to Federal procurement regulations at 24 CFR 85.36, the City did not maintain sufficient records to detail the procurement history for the reimbursements of the previously incurred City street improvement expenses. Since the City's rationale for the method of procurement, selection of contract type, contractor selection or rejection, and basis for the contract price were not documented, the eligibility of the more than \$1.9 million in costs is considered unsupported and is further questioned.

Conclusion

The City disbursed CDBG program funds for questionable street improvement expenditures. Deficiencies identified included that the City used CDBG funds to reimburse its municipal general expense account for ineligible and unsupported City street improvement expenses, did not use CDBG funds to address the community's needs, and did not maintain sufficient procurement records. Consequently, the City's ability to administer its CDBG program efficiently and effectively and ensure that CDBG program objectives were met was diminished. As a result, \$162,923 in ineligible costs and more than \$1.9 million in unsupported costs were charged to the program. We attribute this deficiency to the City's unfamiliarity with HUD regulations, and its circumvention of the regulations and its own policies to expend CDBG funds quickly to prevent a reduction in future funding by HUD.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development

- 1A. Require the City to suspend incurring costs and/or reimbursing itself for costs paid from the City's municipal general expense account for public facilities activities until HUD determines whether the City has the capacity to carry out its CDBG public facilities activities in compliance with HUD regulations.

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

- 1B. Reimburse from non-Federal funds \$162,923 (\$134,711+\$28,212) expended on ineligible costs pertaining to street improvement projects not done and a duplicate reimbursement.
- 1C. Provide documentation to justify the \$1,982,988 in unsupported costs associated with street improvement expenditures incurred between June 2007 and October 2009. Any unsupported costs determined to be ineligible should be reimbursed from non-Federal funds.
- 1D. Establish and implement controls to ensure adequate monitoring of the public facilities/improvement activities.

Finding 2: The City Did Not Adequately Monitor Its Subrecipient-Administered Economic Development Program

The City did not ensure that a subrecipient administering its economic development program had an adequate financial management system and that the performance goals of the activities were achieved. Specifically, the City (1) reported unsupported program income to HUD, (2) charged questionable transactions to the CDBG program income account, (3) could not provide assurances that program objectives were met, (4) failed to safeguard program assets, and (5) achieved minimal progress in its economic development activities. We attribute these deficiencies to the City's lack of monitoring and oversight of its subrecipient. Therefore, it failed to provide fiscal and programmatic monitoring to safeguard the assets of the program and did not take a proactive approach to its oversight of the economic development activities. As a result, it could not provide assurance that more than \$20.1 million in transactions was properly accounted for, CDBG-funded activities met program objectives, and economic development funds were spent in a timely manner, thus depriving other activities of program resources.

Background

The City designated the Buffalo Urban Renewal Agency (Agency) as the entity responsible for the administration of the CDBG program. The Agency contracted with the Buffalo Economic Renaissance Corporation (Corporation) to administer economic development loans and grants. The Corporation was responsible for the development, management, and implementation of a variety of community economic development programs on behalf of the City, including commercial lending, real estate management, and other development projects. In addition to the CDBG program, the Corporation's funding principally came from grants received from the City. The last subrecipient agreements that the Agency executed with the Corporation expired on April 30, 2009. In February 2010, the mayor called for the elimination of the Corporation and the unification of all neighborhood revitalization efforts within the Agency. The Agency's new mission would be to support neighborhood economic development that builds around the commercial cores, with a concentrated effort in the areas of housing revitalization, demolitions, infrastructure improvements, and providing loans and grants to businesses to create strong neighborhoods. The dissolution of the Corporation and the transferring of economic development activities to the Agency were in process as of December 2010.

Unsupported Program Income Amounts Reported to HUD

The City's recording of more than \$4.9 million in economic development program income receipts and expenditures was unsupported. The Corporation maintained all of the program income generated from economic development

activities. In turn, it reported the receipt and expenditure of program income to the City. The City then recorded the transactions in HUD's Integrated Disbursement and Information System (IDIS) and the annual performance reports. However, it did not obtain adequate documentation supporting that the program income had been properly recorded. Regulations at 24 CFR 570.504(a), and 570.501(b) require that receipt and expenditure of program income be recorded as part of the financial transactions of the grant program. The recipient is responsible for ensuring that CDBG funds are used in accordance with all program requirements.

The amounts that the City recorded as program income receipts were unsupported. For fiscal year 2008 receipts, the information submitted by the Corporation to the City consisted of a spreadsheet with no supporting documents. In addition, the Corporation removed the rents received from the program income calculation without explanation. The City accepted the figures on the spreadsheet and reported them to HUD. For fiscal year 2009, the City included an amount for rental receipts after the deduction of rental expenses. However, it did not receive the supporting documentation for the rental expenses to determine whether they were eligible offsets to the rental receipts. Regulations at 24 CFR 570.489(e)(1)(iii) provide that program income includes gross income from the use or rental of real or personal property acquired by the unit of general local government or a subrecipient of a unit of general local government with CDBG funds, less the costs incidental to the generation of the income.

In addition, the amounts that the City reported as expenditures paid with program income were not supported. The majority of the expenditures related to payroll and operations. For payroll, there was no documentation provided for the payroll expenditures for fiscal year 2008 and only timesheets for fiscal year 2009. In addition to the lack of support, there was evidence that unreasonable salary expenditures were charged to the CDBG program during both fiscal years. The CDBG program was charged many hours for unused vacation and sick time of Corporation employees whose termination occurred during the fiscal year. Regulations at 2 CFR 225, appendix B, 8a(1) and 8h, provide that total compensation for individual employees has to be reasonable for the services rendered and conform to the established policy of the governmental unit consistently applied to both Federal and non-Federal activities and be properly supported.

In addition, the City did not provide adequate support for operation costs. The Corporation submitted a number of invoices in which the documentation provided did not support how the cost was allowable. The CDBG program manager agreed that certain expenditures, such as legal fees for personnel actions and expenditures after the fiscal year should not have been charged to the CDBG program during fiscal year 2009. Regulations at 2 CFR 225, appendix A, C(1), provide that to be allowable under Federal awards, costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards. We

attribute the deficiency to the process by which the Corporation submitted invoices for approval by the City after the program income funds had been expended. None of the invoices was submitted to the City for approval until after the end of the fiscal year.

Questionable Transactions Charged to the CDBG Program Income Account

The City could not provide assurance that all CDBG program income receipts were recorded and that only eligible expenditures were paid with program income funds. Specifically, the Corporation recorded more than \$15.2 million in questionable transactions in its CDBG program income account. The transactions represented the receipts, expenditures, and transfers that were recorded during fiscal years 2008 and 2009. We attribute this deficiency to the fact that the Corporation's financial management system did not accurately account for program income transactions and the City's failure to adequately monitor the Corporation's use of program income funds.

The Corporation's financial management system did not accurately account for program income transactions. A review of receipts recorded in the CDBG program income account indicated additional amounts that should have been reported as program income. For example, there was rental income, loan refunds, charge backs, and other miscellaneous revenue that the Corporation should have included as program income that were not reported to HUD during fiscal year 2009. The Corporation's chief financial officer acknowledged that the Corporation did not include all items because of its lack of knowledge of the accounting codes and how certain transactions represented CDBG program income. In addition, the City disallowed a portion of the expenditures paid with CDBG program income that the Corporation submitted to the City for approval in fiscal year 2009. Regulations at 2 CFR 225, appendix A, C(1), provide that to be allowable under Federal awards, costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards. Also, regulations at 24 CFR 570.504(a) and 570.501(b) require that the receipt and expenditure of program income be recorded as part of the financial transactions of the grant program. The recipient is responsible for ensuring that CDBG funds are used in accordance with all program requirements. The use of designated public agencies, subrecipients, or contractors does not relieve the recipient of this responsibility.

The City's failure to adequately monitor the Corporation's use of program income funds provided a lack of assurance that all program income funds were recorded properly and that the expenditures represented eligible costs under the CDBG program. Regulations at 24 CFR 85.40(a) provide that grantees are responsible for managing the day-to-day operations of grant- and subgrant-supported

activities. Grantees must monitor these activities to ensure compliance with applicable Federal requirements and that performance goals are achieved. Grantee monitoring must cover each program, function, or activity. The City could not provide an accurate accounting of the CDBG program income maintained by the Corporation. In turn, the Corporation failed to report monthly program income generated by activities carried out with CDBG funds.

The City's lack of adequate monitoring of the CDBG program income account led to concerns regarding transactions relating to commingled funds and expenditures for non-Federal costs on the Corporation's books and records. The CDBG program income account was commingled with other receipts and disbursements such as CDBG grant drawdowns, Section 108 grant drawdowns, non-CDBG grant funds, and transfers to and from other accounts. In addition, the Corporation made payments from the CDBG program income account that did not relate to CDBG expenditures, raising concerns as to whether these ineligible expenditures were made with CDBG program income funds. For example, the Corporation transferred funds from the CDBG program income account to its payroll account. The transfers represented the total payroll for the Corporation. Likewise, the Corporation used funds from the CDBG program income account to pay the expenditures of its other programs. These expenditures would not be eligible CDBG costs because they related to other programs of the Corporation.

No Assurances That Program Objectives Were Met

The City could not provide assurance that the objectives of the economic development activities administered by the Corporation were achieved. Regulations at 24 CFR 570.501(b) provide that grantees are responsible for determining the adequacy of performance under subrecipient agreements. The City's annual action plans presented performance objectives to be achieved by the Corporation during the respective fiscal year based on the number of businesses and individuals in the community that received assistance through the different programs offered. Specific objectives included job creation related to lending, the number of grants awarded to small, local businesses, and the number of residents that attended entrepreneurial training being offered.

According to the corresponding annual performance report, these goals were not achieved during fiscal years 2008 and 2009. For example, the objective related to lending for both fiscal years 2008 and 2009 was to develop 60 jobs for low- and moderate-income persons by providing low-interest loans to small, local businesses. The Corporation reported that 42 full-time-equivalent positions were created in fiscal year 2008, with 33.5 of these held by low- to moderate-income individuals, and only 4 full-time-equivalent positions were created in fiscal year 2009, with 51 percent of these jobs targeted for low- to moderate-income individuals. Therefore, we attribute the City's inability to meet its goals to a

decline in the number of loans awarded and the lack of adequate oversight by the Corporation. For example, the Corporation closed 13 CDBG-funded loans during fiscal year 2008 and two CDBG-funded loans during fiscal year 2009, thus limiting the number of businesses able to create jobs in relation to loan funding received through the Corporation.

Review of the files provided evidence that Corporation officials did not adequately oversee the activities they funded through the CDBG program. The Corporation's subrecipient agreement, along with its procedures, detailed specific oversight of performance goals that was required to be performed by the Corporation. The majority of businesses with outstanding, active loans through the Corporation were reported as not having provided up-to-date employment creation data. Therefore, the City had no assurances that the loan program met its objective concerning job creation for low- and moderate-income persons. The City was provided activity summary reports for 2009 relating to 28 of 91 active loans in the Corporation's portfolio. Further, nearly half of the active loans in the Corporation's portfolio showed amounts that were more than 90 days delinquent. Thus, the loan files reviewed showed inadequate oversight by Corporation officials evidenced by the lack of required documentation, which in turn contributed to the lack of assurances that program objectives were met.

Failure To Safeguard Program Assets

The City failed to safeguard program assets by not adequately monitoring the efficiency or effectiveness of the Corporation's administration of the economic development activities. As part of its administration of the CDBG program, the City is responsible for the monitoring of its subrecipients. Regulations at 24 CFR 85.40(a) provide that grantees are responsible for managing the day-to-day operations of grant- and subgrant-supported activities. Grantees must monitor these activities to ensure compliance with applicable Federal requirements and that performance goals are achieved. Grantee monitoring must cover each program, function, or activity. The lack of fiscal and programmatic monitoring provided no assurances that CDBG funds were expended in ways that furthered overall program objectives. City officials attributed its lack of oversight over the Corporation to a lack of checks and balances caused by inadequate segregation of duties among its management staff.

The City was unable to provide evidence that it performed fiscal monitoring of the Corporation. Thus, it was unable to ensure the efficiency of the Corporation's administration of economic development activities. The fiscal year 2008 annual performance report referenced that fiscal monitoring of the Corporation had begun during the year but did not continue based upon the absence of a chief financial officer at the Corporation. According to the City's procedures, high-risk subrecipients such as the Corporation are required to be subjected to fiscal and

programmatic monitoring on an annual basis. HUD also expressed the need to monitor high-risk subrecipients during a technical assistance meeting with the City in June 2009. The City provided some evidence of programmatic monitoring, but it did not adequately ensure the effectiveness of the economic development activities administered by the Corporation. Further, comprehensive programmatic monitoring of the Corporation had not been performed by the City since March 2004.

Minimal Progress Achieved in Economic Development

The City achieved minimal progress in its economic development activities. Specifically, it could not ensure that more than \$4.7 million in economic development funds was spent in a timely manner. The City's economic development program was suspended until the City completes the dissolution of the Corporation, implements the revised policies and procedures, and hires personnel capable of providing the neighborhood economic development program that the mayor announced in February 2010. Therefore, as of December 2010, the majority of the CDBG funds for fiscal years 2008, 2009, and 2010 earmarked for economic development projects had gone unspent. Thus, the City should consider reprogramming the remaining funds to put these funds to better use for other eligible program activities.

Conclusion

The City did not ensure that a subrecipient administering its economic development program had an adequate financial management system and that the performance goals of the activities were achieved. Deficiencies identified included that the City (1) reported unsupported program income to HUD, (2) charged questionable transactions to the CDBG program income account, (3) could not provide assurances that program objectives were met, (4) failed to safeguard program assets, and (5) achieved minimal progress in its economic development activities. As a result, it could not provide assurance that more than \$20.1 million in transactions was properly accounted for. In addition, more than \$4.7 million in unexpended funds would result in a cost savings if this amount were reallocated to other eligible activities. We attribute these deficiencies to the City's lack of monitoring and oversight of its subrecipient.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development

- 2A. Require the City to suspend incurring costs and/or reimbursing itself for costs paid from the City's municipal general expense account for economic development activities until HUD determines whether the City has the capacity to carry out its CDBG economic development activities in compliance with HUD regulations. If it is determined that the City lacks the capacity, the \$4,739,829 in economic development projects funds remaining for fiscal years 2008, 2009, and 2010 should be reprogrammed so the City can assure HUD that these funds will be put to better use.

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

- 2B. Provide documentation to justify the \$20,143,219 (\$4,902,754 + \$15,240,465) in unsupported transactions recorded in the CDBG program income account. Any receipts determined to be unrecorded program income should be returned to the CDBG program, and any expenditures determined to be ineligible should be reimbursed from non-Federal funds.
- 2C. Certify and provide support that the proper amount of CDBG assets was returned to the City from the subrecipient by performing an audit of the accounts that the Corporation maintained.
- 2D. Establish and implement controls that will ensure adequate monitoring of subrecipient-administered activities, that CDBG funds are properly safeguarded, the achievement of performance goals in subrecipient supported activities, and that corrective actions are taken for nonperforming subrecipients.

Finding 3: The City Charged Ineligible and Unsupported Costs for Clean and Seal Program Activities to its CDBG Program

Contrary to HUD requirements, the City did not establish adequate administrative controls to ensure that costs associated with its clean and seal program were allowable and supported by sufficient documentation before being charged to the CDBG program. Specifically, it could not demonstrate that more than \$1 million in CDBG funds spent to board vacant buildings and clear vacant lots under its clean and seal program were properly supported or represented eligible activities that met a national objective. We attribute these deficiencies to the City's general unfamiliarity with HUD's regulations pertaining to clearance activities. As a result, ineligible and unsupported costs were incurred, and the City's ability to ensure that CDBG program objectives were met was diminished.

Background

The primary purpose of the City's clean and seal program is to board up vacant buildings and clean properties of debris throughout Buffalo. Requests for a vacant building board up or cleanup comes from various sources, including the City's court judge, housing inspectors, citizen complaints, council members, and/or the police and fire department.

City officials expended more than \$1 million in fiscal year 2008 and 2009 funds on its clean and seal program for employees' salaries and material/supply costs during the review period. Therefore, we examined all of these activities to determine the reasonableness of the costs and the City's compliance with applicable program requirements. For each of the fiscal years reviewed, administrative weaknesses were identified that resulted in costs having been incurred that were ineligible and/or unsupported. Particulars regarding the review of each fiscal year are discussed below.

Fiscal Year 2008 Clean and Seal Program

Review of the project activity files for the City's fiscal year 2008 clean and seal program in which employee payroll and material/supply costs were charged to the program revealed that City officials expended \$545,607 on the City's 2008 clean and seal program, having incurred \$518,779 for employee payroll and \$26,828 for material/supply costs.

The City classified its fiscal year 2008 clean and seal program as a clearance activity, thus eligible for funding under CDBG program regulations at 24 CFR 570.201(d). However, to qualify as a clearance activity under the program regulations, the City would be required to demonstrate that the properties affected

were later demolished. Contrary to this requirement, the City provided a list of 1,503 property addresses for which a board up or cleanup had occurred. While the City maintained supporting documentation to show that a property boarded up or vacant lot cleanup had occurred at the addresses included on the list, it was unable to provide documentation to show that any of the properties included on the list had been or were planned to be demolished within a reasonable timeframe. Moreover, there was no coordination between the City's demolition department, which is responsible for all demolition activity throughout the City, and the clean and seal program. City officials stated that when a vacant property was boarded up under the clean and seal program, it did not mean or require that the property would be demolished. Further, examination of the list determined that many addresses appeared on the list more than once, indicating that the clean and seal employees were sent to some properties more than once during the fiscal year to perform a board up and/or cleanup.

Based on analysis, the costs incurred appeared to characterize general government and maintenance expenses. According to CDBG program regulations at 24 CFR 570.207(a)(2), expenses required to carry out the regular responsibilities of the unit of general local government are not eligible for assistance under this part. Since the City could not demonstrate that its clean and seal program represented a clearance activity, as required by the program regulations, and instead appeared to be a program that was part of the City's regular responsibility, we considered the use of \$545,607 in CDBG funds used for clean and seal salary and material/supply costs to be unsupported.

Fiscal Year 2009 Clean and Seal Program

As part of its review of the City's 2009 annual action plan, HUD advised the City that for the clean and seal program to be eligible as a clearance activity, the property would later have to be demolished. Further, HUD requested that the City submit additional information to clarify whether the program was tied to property demolition and if not, explain how it would fit into another CDBG eligibility category. While the City responded to HUD, it did not directly address how its clean and seal program was tied to property demolition and continued to administer its program as it had during the previous year.

Initially, the City had classified its fiscal year 2009 clean and seal program as a clearance activity and produced a list of 1,422 properties for which a board up or cleanup had occurred. However, to comply with HUD's directive, the City reclassified its clean and seal program as qualifying under other CDBG-eligible categories. Specifically, properties were reclassified to qualify under code enforcement, rehabilitation, or clearance (slums/blight and low/mod). Moreover, based on reclassifying the eligibility criteria, the City determined that 187 properties

no longer qualified for the program, resulting in \$78,962 in salary and material costs' being reimbursed to the CDBG program from non-Federal funds.

Ineligible Costs Charged for Code Enforcement Activities

City officials determined that \$304,506 in clean and seal program expenditures qualified as a code enforcement activity under CDBG program regulations at 24 CFR 570.202(c). According to City officials, these were properties for which the request for a board up or cleanup was made by one of the City's housing inspectors and the board up or cleanup was performed in conjunction with a code enforcement activity. In addition, the properties were located in targeted areas in which the City had other improvements underway.

On May 14, 2009, HUD issued a memorandum outlining the provision that boarding up vacant buildings may also be classified as code enforcement under CDBG program regulations at 24 CFR 570.202(c), provided this activity is carried out as part of a code enforcement effort and along with other activities such as public improvements, rehabilitation, and services which are expected to arrest the decline of the area. CDBG program regulations at 24 CFR 570.202(c) detail requirements regarding code enforcement activities and provide that CDBG funds can be used for costs incurred for inspection for code violations and enforcement of codes, specifically, the salaries and related expenses of code enforcement inspectors and legal proceedings, but not including the cost of correcting the violations.

Based on our review, the costs incurred for the clean and seal code enforcement activity represent the salary and material costs of the clean and seal crew to board vacant buildings and clean vacant lots, in other words, the cost of correcting the code violations. Accordingly, the \$304,506 charged to the CDBG program for the clean and seal code enforcement activity to correct code violations was considered ineligible.

Unsupported Rehabilitation and Clearance Costs

City officials reclassified 57 properties for which a board up had occurred as an eligible rehabilitation activity under CDBG program regulations at 24 CFR 570.202(a). These 57 properties were occupied and represented properties for which some form of building permit had been applied for from the City's Department of Permit and Inspection Services. However, City officials stated that none of the properties was included in the City's CDBG-funded rehabilitation program, and there was no documentation to show what type of rehabilitation, if any, had been completed on the properties. Accordingly, we considered the \$24,069 in clean and seal program expenditures for rehabilitation activities to be unsupported since the

reclassified code enforcement activities were not carried out along with other activities in accordance with CDBG program regulations at 24 CFR 570.202(a) as noted above.

In addition, City officials determined that \$146,947 in fiscal year 2009 clean and seal program expenditures still qualified as a clearance activity. The City had the properties added to its demolition department's list of properties to be demolished. While approximately 45 of the properties were already included on the demolition department's list, approximately 300 more were added. Although there were 345 properties included on the list, we were told by City officials that there was no assurance that these additional properties would all be demolished. Therefore, as with the City's fiscal year 2008 clean and seal program, City officials did not adequately demonstrate that the program represented an eligible clearance activity as required by the program regulations. Accordingly, we considered the use of \$146,947 in CDBG funds used for clean and seal salary and material/supply costs associated with these properties to be unsupported. According to City officials, the questionable clean and seal program activity costs were attributed to a lack of clarity amongst the Agency and various City departments that demolition was to be the ultimate goal of properties that were boarded and/or cleaned up.

Conclusion

Review of the City's administration of its clean and seal program activities revealed that adequate controls were not established to ensure that costs were eligible and necessary before being charged to the CDBG program. Consequently, the City expended \$304,506 for ineligible purposes and \$716,622 (\$545,607 + \$24,069 + \$146,946) for unsupported costs, thus diminishing its ability to ensure that its program was administered in an effective and efficient manner. We attribute these deficiencies to the City's general unfamiliarity with HUD's regulations pertaining to clearance activities.

The City also allocated \$744,479 in fiscal year 2010 CDBG funds for its clean and seal program. However, if it cannot demonstrate how its clean and seal program will comply with program requirements, these funds should be reprogrammed for other eligible purposes and put to better use.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Community Planning and Development

- 3A. Require the City to suspend incurring costs and/or reimbursing itself for costs paid from the City's municipal general expense account for clean and seal activities until HUD determines whether the City has the capacity to

carry out its CDBG clean and seal activities in compliance with HUD regulations. If it is determined that the City lacks the capacity, \$744,479 in fiscal year 2010 clean and seal program funds should be reprogrammed so the City can assure HUD that these funds will be put to better use.

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

- 3B. Reimburse from non-Federal funds the \$304,506 related to ineligible clean and seal code enforcement costs.
- 3C. Provide documentation to justify the \$716,622 (\$545,607 + \$24,069 + \$146,946) in unsupported clean and seal costs incurred so that HUD can make an eligibility determination. Any costs determined to be ineligible should be reimbursed from non-Federal funds.
- 3D. Develop administrative control procedures that will ensure compliance with CDBG program requirements, including ensuring that costs are eligible and necessary before being charged to the program.

SCOPE AND METHODOLOGY

We performed onsite audit work at the City's offices in City Hall, located in Buffalo, NY, between June and December 2010. The audit scope covered the period May 1, 2008, through April 30, 2010, and was extended as necessary. We relied in part on computer-processed data primarily 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. To accomplish the objectives, we

- Reviewed relevant HUD regulations, guidebooks, and files.
- Interviewed HUD officials to obtain an understanding of and identify HUD's concerns with the City's operations.
- Reviewed HUD's March 2009 monitoring report, which was the basis for the complaint. The report identified 19 findings including a lack of operating procedures and a clear organizational structure for the CDBG program, and questionable costs charged to the CDBG program of more than \$4 million.
- Reviewed the City's policies, procedures, and practices.
- Interviewed key personnel responsible for the administration of the City's CDBG program.
- Tested expenditures in the public facilities and improvements, economic development, and clearance program areas. Specifically, we used nonstatistical sampling for our selection of (1) public facilities and improvements, (2) economic development, and (3) clearance program area transactions. For fiscal years 2008 through 2010, the City received approximately \$49.3 million in CDBG funding. HUD's Integrated Disbursement and Information System reports reflect that more than \$28.4 million in CDBG funds was disbursed for 566 activities for fiscal years 2008 and 2009. These program areas represented more than 42 percent of the City's CDBG funds budgeted in these 2 years. Therefore,
 1. For the public facilities and improvements program area, we reviewed each of the 11 expenditures occurring on February 23, 2010, the date \$2.1 million was reimbursed to the City from CDBG funds for street improvement projects.
 2. For the economic development program area, we performed a detailed review of program income transactions occurring during two 2-month periods, May through June 2009 and March through April 2010. We performed a comprehensive review of program delivery and administrative expenditures relating to economic development activities. Also, we reviewed 10 active loans from the Corporation's commercial lending portfolio. The Corporation had an active portfolio of 91 loans with a balance of more than \$6.6 million as of May 31, 2010.

3. For the clearance program area, we reviewed all 2008 and 2009 expenditures occurring during our audit period.

The results of our testing only apply to the transactions reviewed and cannot be projected to the total population of CDBG transactions.

- Reviewed all documentation supporting the economic development program delivery and administration transactions for fiscal years 2008 and 2009.
- Reviewed the transactions charged to the CDBG program income account maintained by the Corporation.

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

- The City did not have adequate controls over the effectiveness and efficiency of program operations when it did not establish adequate administrative controls to ensure that costs associated with public improvement, economic development, and clearance activity were supported and eligible under the CDBG program (see findings 1, 2, and 3).
- The City did not have adequate controls over compliance with laws and regulations, as it did not always comply with HUD regulations while disbursing CDBG funds (see findings 1, 2, and 3).
- The City did not have adequate controls over safeguarding of resources regarding its economic development subrecipient that retained and expended program income (see finding 2).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1B	\$162,923		
1C		\$1,982,988	
2A			\$4,739,829
2B		\$20,143,219	
3A			\$744,479
3B	\$304,506		
3C		\$716,622	
Total	\$467,429	\$22,842,829	\$5,484,308

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.

3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (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, if the City implements our recommendations to (1) reprogram the remaining economic development project funds if it is determined that the City does not have the capacity to carry out its economic development activities, and (2) develop control procedures to ensure program compliance for future clean and seal activities, it can assure HUD that these funds will be properly put to better use.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



BYRON W. BROWN
MAYOR

CITY OF BUFFALO
DEPARTMENT OF ADMINISTRATION,
FINANCE, POLICY & URBAN AFFAIRS



JANET E. PENKSA, Ph.D.
COMMISSIONER

March 10, 2011

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

RE: Written Comments to Draft Audit Report (cover letter dated February 17, 2011)

Dear Mr. Moore:

Comment 1

We appreciated the opportunity to review the Draft Audit Report with your staff during our exit conference on March 8, 2011. We recognize that the Office of Inspector General (OIG) has reviewed a number of matters, but we believe that OIG has reached subjective conclusions in many instances, and in other instances did not reach conclusions supported by the information provided. Moreover, OIG does not appear to have fully recognized the reorganization that the City of Buffalo (the "City") has already performed, addressing a wide variety of issues. As such, we request that OIG review the information, provided at the exit conference and in this letter, and revise the Draft Report and hold a further exit conference.

Comment 2

Comment 3

At the exit conference, we were told by OIG staff to keep our response to three pages per finding. We do not believe such page limits assist in a full and fair review of the important matters under review and request that no portions of this response be paraphrased or redacted.

Comment 4

The OIG Draft Report primarily addresses administrative and records management of the City of Buffalo Urban Renewal Agency (BURA). The Draft Report does not appear to adequately address the fact that there has been substantial operating and staff changes. Indeed, the Draft Report pertains to a period in which prior administrators were in place. Since then, the Mayor has removed most of these administrators and sought authorization to dissolve its primary economic development agent as a result of a thorough review he asked me to conduct. Our response attempts to identify and acknowledge the areas of deficiency on the part of the prior administrators and share corrective actions taken to date.

Comment 5

Our review is ongoing, comprehensive, and methodical. Corrective actions are made carefully and deliberately to ensure compliance and sustainability and adopted only after thorough review by the City and HUD's Buffalo Field Office. Our commitment to assuring the use of Community Development Block Grant funding is compliant with HUD regulations and meets the needs of the community is demonstrated by the February 2009 clearance of 19

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Comment 5

findings made by the Buffalo Field Office earlier that year and our adherence to a schedule of weekly meetings with that office for review and sign-off on items of concern. The continued assistance of the OIG is an important component of this ongoing process.

Comment 6

The supporting exhibits referenced in this response are produced under separate cover. Due to the volume of this additional documentation, the exhibits will be provided to the offices of the OIG located at 465 Main Street, 5th Floor, Buffalo, New York 14203 via hand delivery on March 11, 2011.

Preliminary Statement

Comment 6

The City is committed to administering its Community Development Block Grant Program (CDBG) to clearly address the needs of our community in accordance with HUD requirements and correcting any fact-based findings to the contrary. The Draft Report in several places states that supporting documentation was not provided, but as we note below, that information was provided and we respectfully ask that the final report reflect that fact.

Comment 7

The findings and recommendations related to reimbursements to the City for street improvement expenditures (Finding One) should be reconsidered given that all of these costs were associated with street improvements in eligible areas, including those claimed to be located in substantially industrial or non- low income census tracts. HUD Regulations at 24 CFR 570.201(c) and (f) specifically includes street improvements as a basic eligible activity.

Comment 8

Moreover, discouraging basic infrastructure improvements such as these ignores that, as a policy matter, the City is an older industrial city with neighborhoods historically clustered around industrial sites so workers could easily access job sites. Faulting the City for making street improvements in these areas fails to consider the community's needs for safe streets so that neighborhood residents, particularly children, can safely access schools and services.

Comment 9

The recommendations related to monitoring of the Buffalo Economic Renaissance Corporation ("BERC"), the economic development subrecipient, (Finding Two) should be reconsidered in light of the fact that BURA took substantial corrective action prior to the audit field work and at the direction and cooperation of the former Director of Community Planning and Development Division of the Buffalo Field Office (Buffalo Field Office).

Comment 10

After discussions with the auditors at the pre-exit conference with OIG on December 17, 2010, the City discovered that the on-site field work did not include a review of vital information. The pre-exit conference was the meeting between City and OIG staff after OIG concluded its field work but before the Draft Report was provided. After that meeting we provided our December 20, 2010 letter providing explanations and certain documentation, and requested the continuation of field work. However, it appears as if OIG did not consider the information in that letter prior to issuing its report.

Comment 11

Contrary to the findings contained in the Draft Report, the City actively monitored the activities of BERC in 2008 and 2009, and, based on this monitoring, determined that it would end its subrecipient agreement with BERC. As a result, the Mayor announced in February 2010 that he would begin to dissolve the agency and on May 1, 2010, the beginning of the next block grant program year, the City's Commissioner of Administration and Finance

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Comment 12

conveyed written correspondence to BERC officials notifying them to return all program income and that further block grant funding would not be made available. See **Exhibit A**. Since then, all BERC program income has been returned to the City despite having incurred eligible program expenditures, none of which have yet to be charged to the block grant.

Comment 13

The recommendations related to the City administration of the clean and seal program (Finding Three) should also be reconsidered because HUD's own directives consider these to be eligible activities. Prior to the audit field work and through to the present, the City has maintained sufficient documentation to evidence eligibility. The Buffalo Field Office raised the issue of providing documentation as to length of time between clean and seal and eventual demolition. After it was determined that the speed of demolitions was insufficient, the City directed its clean and seal efforts to code enforcement with the assurance that these were eligible activities. The City proceeded based upon this guidance and the attached HUD directive which clearly states that "Boarding up vacant buildings may also be classified as part of a code enforcement effort". Moreover, HUD regulations at 24 CFR 570.202(c) provide that costs incurred for inspection of code violations, including salaries and related expenses of code enforcement inspectors and legal proceedings are eligible activities. Stabilizing a property and sealing it are not correcting the violation, such as rehabilitation, would accomplish.

Comment 14

Statements regarding whether or not the City met community needs appear in the Draft Report. The City's position is that these conclusions are premature in light of the volume of data that was not considered during the field work. During the audit, the City produced required documentation supporting the proper use of federal funds when they were requested. Upon the exit interview, we easily located additional documentation that would have been material to the audit and upon review of the Draft Report, we once again easily located documentation that contradicts numerous conclusions.

Response to Finding One

**City Street Improvements Served the Community's Needs,
Were Properly Performed, Documented and Charged to the CDBG Program**

The sections of Finding One are addressed below:

Comment 15

A. Courtland Ave. from E. Delavan to Easton \$28,680.04 (Lovejoy), \$28,211.84 (University), IDIS 7509 CD 509-34

BURA did not pay for the same work twice as the Draft Report alleges. Courtland Avenue is listed under two different council districts on the City's streets list, Courtland Ave. from E. Delavan to Easton St. borders the University District on the west side and the Lovejoy District on the east side. In order to reflect the cost of the street attributed to each council district, the cost of mill and overlay for this street was apportioned between the two districts. Both the City and BURA use a geographic information system (GIS) for planning and reporting purposes. A map that reflects the council district boundaries and the vouchers for Courtland under each district are provided as **Exhibit B**.

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Auditee Comments

Comment 16

B. West Parade from Northampton to East North \$14,513.09 (Ellicott) IDIS 7509 CD 509-34

This project was a reimbursement for work that was bid through the City. The original streets list inadvertently reflected West Parade from Northampton to East North instead of from Northampton to Best for \$41,982.54. This was a typographical error made in entering the street names on the list. West Parade runs from Northampton to Best Street and does not intersect with East North. See map provided in **Exhibit C**. BURA reimbursed the City for mill and overlay on West Parade from the Kensington Expressway to Best.

The total cost of the work on West Parade from Northampton to Best was \$41,982.54. BURA reimbursed only a portion of the work in the amount of \$14,513.09 for work done on West Parade between the Kensington Expressway to Best Street (Census Tract 35, Block Group 6). This census tract and block group has a population comprised of 79.7% low to moderate income persons. The amount BURA paid to the City was reduced and adjusted for a smaller section of work done on West Parade graded as an eligible, low/mod area. BURA reimbursed the City for the cost assessed for this portion of the street and has made this correction in its records. On January 14th, 2011, BURA's in-house engineer, along with a representative from Marquis Engineering, the consultant that provided the architectural/engineering for this work, went out to the site on West Parade and verified that the work BURA paid for was completed. See correspondence from Marquis Engineering and voucher for \$14,982.54 provided in **Exhibit C**.

Comment 17

C. Academy Road Curb Replacement (\$56,223 IDIS 7506, CD 500-35 and \$57,777 IDIS 7505. CD 508-34)

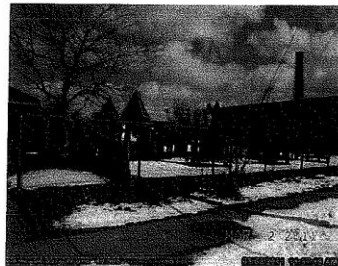
This street was inadvertently included in a list of projects that were deemed to be complete, yet the City did not expend the funds, instead held the funds until the work was complete. The City has fully repaid BURA in the amount of \$114,000 for the Academy Road curb replacement. BURA made adjustments to its records to reflect the reduction of this expenditure and return of funds. In order to prevent this from occurring in the future, BURA has revised its policy manuals to require photographic evidence of all physical development projects be produced prior to payment. See the City of Buffalo Office of Strategic Planning Policy & Procedures Manual provided as **Exhibit D**.

Comment 18

D. Improvements made on Urban and Amherst Streets:

Urban Street

The City disagrees that this project only benefited an industrial area. The Draft Report referenced a photograph of Urban Street facing *east* on page eight (8) of the report to bolster that position. We performed a site visit and obtained additional photographs. The photographs below depict the same area on Urban Street, but facing *west*:



Comment 18

Illustrated by the above photos (and additional photos provided as Exhibit E), the area is not primarily an industrial site as claimed in the Draft Report, but contains a park, community center, school and residential dwellings. The photo in the Draft Report of an industrial site used to justify the finding represented only one side of the street while neglecting to show the non-industrial areas, which is misleading. Across the street from this site is a school and nearby are a playground and a key public service agency.

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Auditee Comments

Comment 18

The census data for the area encompassed by Urban Street., from Moselle to Kehr clearly meets HUD regulations governing the use of block grant for low and moderate income purposes and is as follows:

Urban Street (north side) = Census Tract (CT) 35 Block Group (BG) 2 reflects 279 Low Moderate Income Persons (LMIP) out of a population of 414 people for a LMIP benefit of 67.3%

Urban Street (south side) -- Census Tract 35 BG 3 reflects 71 LMIP out of a population of 72 persons for a LMIP benefit of 98.6%

This demonstrates compliance with 24 CFR 570.200(a) (2) & 208(a) as it benefits low and moderate income families.

At the east end of Urban Street at the corner of Moselle is the CRUCIAL Community Center and the Genesee Moselle Counseling Center. A string of residential homes on Urban St. is located across from the centers with BUILD Academy Elementary School backing up to these homes. There is also a large playground with multiple play structures just down the street from the Community Center. Between this playground and the community is a large apartment complex. While there are light industrial buildings in the middle of the block, there is again housing at the West end at the corner of Urban & Kehr. If you proceed down Urban Street, past Kehr, there are additional residential homes. Residents on Urban Street, Kehr Street, French St. and Fougerson will travel down Urban Street to access the Community Center, playground, and school. There are a total of 350 people living in the two block groups that border this street. To restrict the use of CDBG funds in this area would deprive this neighborhood of improved access to schools, playgrounds, and human services.

Moreover, the CDBG program was created to provide public improvements that benefit both businesses and/or residents.

In summary, this was an eligible project located in an eligible area that served low/mod income residents and served community needs.

Amherst St.

The City disagrees that this project only benefited an industrial area. The Draft Report inserts on page 9 a photograph of one section of Amherst Street that runs underneath a rail road above grade crossings, which is misleading. Many areas of the City have similar viaducts constructed in order to reduce accident risks in primarily residential areas with railroad crossings at grade. Amherst Street is a secondary artery road that crisscrosses northern Buffalo for miles. The specific site funded with CDBG funds is a small strip at the end of a residential neighborhood bordering Amherst St., Thompson, Saint Francis St., and East Streets. The photograph inserted below accurately depicts the area:

Comment 18



Comment 18

The portion of Amherst Street improved by CDBG funds is located in two main Census Tracts. The Census Data is as follows:

CT 59 BG 5 - 491 persons, 285 LMIP, 58.0% LMIP Benefit
CT 59 BG 6 - 458 persons, 393 LMIP, 85.8% LMIP Benefit

This strip connects neighborhood residents to local business and retail. Just east of the viaduct, residents travel to get to the Tops grocery store located on Grant and Amherst. East of the viaduct are neighborhood businesses such as M&T Bank, Pinnacle Automotive and various food services. Maps reflecting these areas are provided as **Exhibit F**.

This portion of Amherst Street is not industrial but connects the low/mod income residents to the neighborhood's commercial district and clearly addresses the community's needs by providing safe access to important services. This portion of the road was in extremely poor condition and unsafe for pedestrian use.

In summary, this was an eligible project located in an eligible area that served low/mod income residents and community needs.

E. Improvements to the Delaware District:

Comment 19

The City replaced sidewalks on the south side of West Ferry from Delaware to Linwood at a cost of \$10,153.65. The census data for this area is as follows:

CT 6602 BG 3 - 722 persons, 528 LMIP, 73.1% Low/Mod Benefit

Ref to OIG Evaluation

Auditee Comments

Comment 19

The City's Consolidated Plan for 2008 through 2012 includes a map on page 7 of Census tracts and block groups that are low/mod income areas of the City used as a basis for geographic distribution. The City's HUD approved Consolidated Plan also is based on the City's Summary of Neighborhood Conditions which rank neighborhoods based on the following:

Neighborhoods ranked as "Poor" should be targeted for Restructuring
Neighborhoods ranked as "Fair" should be targeted for Revitalization; and
Neighborhoods ranked as "Good" should be targeted to Reinforcement

The Summary of Neighborhood Conditions was also utilized in preparing the City's HUD approved Livable Communities Plan. While the City does not use CDBG funding for any high income areas in the Delaware District, there are areas of this district that are occupied by low income residents. This area of West Ferry has a population that is 73% low/mod residents living below the poverty level. The City's Annual Action Plan also emphasized that this funding would only be used for public improvements in low/mod income areas. As such, this was an eligible use of CDBG funding. Also, what the photographs fail to show is that at the corner of Delaware and West Ferry are several multi-family housing structures. See Exhibit G. 1165 Delaware Avenue occupies the northeast corner. It is a four story apartment building, owned by 1165 Delaware Associates LLC and serves low income and senior citizens. The Southeast Corner contains a three story apartment building (1149 Delaware Avenue) owned by Myron Robbins which our initial research identifies to be market rate housing.

F. Meeting Community Needs:

Comment 20

The City's Consolidated Plan lists infrastructure improvements including street and sidewalk improvements as a High Priority Need. See Exhibit H. Buffalo is an older city with and as such its infrastructure requires a high level of which is considered important to addressing the community's needs for safe access to schools, playgrounds, and service. The Consolidated Plan also provides a map of low/mod income areas for the basis of distribution on page 7. The Consolidated Plan provides for the use of CDBG funding for street and sidewalk improvements in low/mod income areas of the City.

Traditionally, streets and sidewalk improvements were bid out by the City and then reimbursed by the CDBG Program. This was done to obtain greater economies of scale by combining both low/mod income areas as well as other non-low/mod areas that were in need of these improvements that were funded by capital bonds or general City revenues. With the state of the economy so poor, now more than ever, the City must rely on whatever cost saving measures it can to maintain its infrastructure. In addition, Part 85 Administrative Requirements for Grants and Cooperative Agreements to State, Local and Federally Recognized Indian Tribal Governments, states under 85.21 Payment - Paragraph (d) Reimbursement, that "Reimbursement shall be the preferred method when the requirements of paragraph c (Advances) of this section are not met." See Exhibit H. The fact that CDBG reimbursed the City for this work was compliant with HUD regulations and does not diminish the fact that CDBG funds were used to improve its infrastructure in its low/mod income neighborhoods and helped to meet community needs.

Ref to OIG Evaluation

Auditee Comments

Comment 20

All of the streets that were reimbursed for street and sidewalk improvements were located in low/mod income areas of the City. This was documented by maps and census data in the City's CDBG project files. The City would also like to note that the lowest level of census data available for entitlement cities is at the block group level and that this data is approved for use by HUD. We have also provided this documentation as **Exhibit I**. The City has also changed its policy manual to include photographic documentation and on site monitoring before reimbursement of any future work.

Comment 21

G. Procurement Documentation

The City bids all of its construction contracts through a formal bidding procedure. Bids are reported to the Common Council and approval is granted by the Council. The OIG had access to all records and personnel related to the procurement of this work and the Record of Common Council Proceedings, which included this information, was made available to the auditors. The complete procurement documents are provided as **Exhibit J**.

In the future, public improvements funded by the CDBG Program will be bid out directly by or under the supervision of BURA staff in order to better control this process from commencement to completion. Street selection is based on City Department of Public Works analysis of conditions and needs and is reviewed by the CDBG Program Manager for eligibility and consistency with the Consolidated Plan. The Program Manager signs the item presented to the BURA Board for approval certifying eligibility. Sites for improvements will continue to be carried out in areas that are primarily residential and are also populated with over 51% low to moderate income residents per 24 CFR 570.208. As is the current practice, the BURA in-house engineer will act as project manager to review contractor work, and process payments. BURA will also continue to handle procurement in accordance with CDBG regulations and will fund the engineering contract that monitors the contractor work. There will also be before and after pictures of each improvement that will be submitted with each voucher for payment.

Response to Finding Two

Documentation is Available to Qualify Subrecipient Expenditures, Monitoring and Corrective Action was Taken, and Economic Development Activities Are Ready to Move Forward

The following is a general response which addressed all of the information contained in Finding Two.

Comment 22

The OIG had access to all of the records necessary to review alleged unsupported transactions. BEREC maintains hard copy and electric records for each transaction cited in the Draft Report. In fact, in a November 19, 2010 email, OIG acknowledged receiving two CD ROMs containing vouchers from BEREC. As such, the Draft Report should unequivocally state that documentation to support each transaction was available for review by OIG during the audit.

Comment 23

In addition, the Draft Report should clearly note that for 2008 BURA and BEREC operated as one entity through its common CFO and access to the Laserfiche document scanning system.

Ref to OIG Evaluation

Auditee Comments

Comment 23

Given this administrative structure and common document archiving system, the Draft Report should remove any findings related to the lack of records maintained by BURA required to support the transactions cited. Absent such removal, the Draft Report should acknowledge such operational structure and that while any records sought from BURA may have been maintained in BEREC's files, the City did not believe it necessary to undertake the expense both dollar value and environmental, to cause a duplicate set of records be maintained in both locations. And that it is reasonable to accept that BURA directly monitored each transaction cited in the Draft Report for 2008.

Comment 24

The Draft Report should further acknowledge that the City (a) began to reorganize and separate the administration of BURA and BEREC in July 2009 and (b) decided in February 2010 to end the subrecipient relationship with BEREC. From a monitoring and reporting perspective in 2009, the Draft Report should note that BURA (i) requested all vouchers from BEREC except those related to normal and ordinary direct real estate expenses and (ii) upon production by BEREC, BURA reviewed these vouchers to determine the eligibility of each transaction where judgment is required.

Given these facts, the City believes that all information was available for review by BURA and OIG and therefore all allegations to the contrary contained in this Finding Two should be removed in their entirety.

Below is a more specific response which responds to the sections of Finding Two in the order that they appear in the Draft Report.

A. Program Income Support (\$4.9 million)

Comment 25

The City strongly disagrees with the finding that \$4.9 million of economic development program income and receipts were unsupported. As stated above, all of the information necessary to support the recording of economic development program income and receipts was available to both BURA at the time of reporting and to OIG during the audit. During the time covered by the audit, BURA had common access to all records, and in particular, the Laserfiche scanning system that BEREC uses to archive documents. All real estate expenditures were available for 2009 and subsequently, BEREC provided BURA and OIG with a CD ROM that contained all checks for 2009, including the real estate checks. Clearly, the information is readily available for review and, as such, this finding should be removed.

Comment 26

BEREC is now required to provide BURA copies of the necessary documentation to support all of the income and disbursements reported to HUD, rather than allowing them to be available for review as was done in the past.

Comment 27

With respect to the finding relating to payroll, the City respectfully requests that it be removed because both BURA and OIG had access to the information to support the expenditures. BEREC provided OIG with information requested in its initial email dated July 29, 2010 in three separate transmissions totaling 687 pages.

On December 7, 2010, electronic copies of payroll records for fiscal years ending 2007 through 2010 were sent to OIG. Given that OIG had access to these detailed records, it would

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Comment 27

have been able to both find that sufficient information was available to support the expenditures and review whether those expenditures were eligible. At a minimum, if OIG chooses not to remove this finding, the City respectfully requests that the references to eligibility be removed as HUD has acknowledged that it has not yet undertaken this review.

Comment 28

As it pertains to the OIG finding of excessive staff benefit reimbursements, BURA requested and BEREC complied, by providing reimbursement from non-federal funds in an amount paid to a former employee for accrued time owed at the time of separation. This payment in no way concedes that such payment was not an eligible block grant expense as it conformed to the policies and procedures in place at the time and such policies and procedures were consistently applied to both federal and non-federal activities.

Comment 29

With regard to other invoices questioned by OIG as to eligibility, the City respectfully asks that these findings be reconsidered in the final report because OIG stated in its Draft Report that it had not yet reviewed the records. As such, any finding along these lines would be premature and not serve anyone's interest.

Comment 30

Lastly, the methodology employed by the auditors to arrive at a finding that \$4.9 million of the City's reported economic development program income and receipts is unsupported and is based on the unconventional method of combining both debits and credits. This methodology has the effect of vastly overstating the significance of the unsupported amount in that it implies that the City expended \$4.9 million of federal money that may be ineligible. In reality, in speaking with the auditors, it was acknowledged that the unsupported number was calculated by adding \$3.1 million in receipts and \$1.8 million in expenditures, thus any potential exposure is far less than \$4.9 million. If OIG chooses not to remove this finding, the City respectfully requests that OIG explain its methodology so any reader is not misled to believe the City's exposure is \$4.9 million.

Comment 31

B. Transactions to the CDBG Program Income Account (\$15.2 million)

The City strongly disagrees with the finding that BEREC recorded more than \$15.2 million in questionable transactions in its CDBG program income account. As stated above, all of the information necessary to support the recording of transactions in the CDBG program income account was available to both BURA at the time of reporting and to OIG during the audit. During the time covered by the audit, BURA had common access to all records, and in particular, the Laserfiche scanning system that BEREC uses to archive documents. Clearly, the information is readily available for review and, as such, this finding should be removed.

During the audit, OIG requested account histories for the period from May 1, 2008 to April 30, 2010 from BEREC's CDBG Program Income Account [REDACTED] as an additional information request once it had been on site for many months. BURA, through BEREC, provided an electronic download of this data from BEREC's Great Plains accounting system on September 13, 2010.

BEREC's submission of the Excel Spreadsheet that contained Account [REDACTED] information is evidence that transactions were supported and reasonable, conforming to consistent presentation of business operations for loan processing, rental collections, the receipt of certain grants, and the expenditure of funds for payroll, benefits, and normal

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Comment 31

operating and maintenance requirements of the real estate operations owned and managed by BEREC. The Excel Spreadsheet contained 3,580 rows of financial information with columnar data that included debit amount, credit amount, journal entry number, originating master, and reference. Of these columnar categories, the journal entry number, originating master, and reference provided clear record of the source or use for each transaction.

As in the case in Section A, above, the Draft Report followed a similar procedure of adding these debits and credits to arrive at its estimate of “unsupported” transactions of approximately \$15.2 million rather than netting debits and credits and narrowing the list to items which required supplemental information not contained in electronic format. As stated earlier, this methodology has the effect of inflating the claimed unsupported amount.

Comment 32

When the City was provided the pre-exit interview by OIG and received indications of its concerns and a verbal description of the methodology used to review the CDBG Program Income Account on Friday, December 17, 2010, the City provided a detailed letter to HUD on Monday, December 20, 2010, which (1) questioned the methodology used to calculate Program Income, (2) provided copies of Internal Bank Transfer documents, Check Request details, which demonstrated the intended funding source for each transaction, and associated Bank Statements that OIG had not reviewed, and (3) requested that additional follow-up work could occur so that the letter and its 279 pages of supporting information could be reviewed.

In light of the City’s immediate response and delivery of un-reviewed materials, the City strongly disputes the fact that these \$15.2 million of transactions were “unsupported” or “questionable” because (a) the electronic format provided to OIG early in its review contained journal entry numbers, originating master, and reference information that provide direct evidence of the intended source and use for the transactions and (b) supplemental information provided in the December 20, 2010 letter provided sufficient information to address any concerns that could not be resolved with data provided electronically.

C. Assurances that Program Objectives Were Met and Program Assets Safeguarded

The City has consistently sought assistance from HUD, including requests for technical assistance, to assure compliance with HUD regulations and meeting and exceeding set program goals.

Comment 33

The City took corrective actions to safeguard assets in the control of BEREC, including but not limited to, discontinuation of all CDBG funding to BEREC, recovery of Program Income, and escrow of non-federal monies held by BEREC. This action was taken as a result of extensive program monitoring performed by the City during the 2009 fiscal year.

The Draft Report criticizes the City for not adequately monitoring its subrecipient, BEREC, yet fails to recognize that the Mayor’s reorganization of its economic development programs came as a result of the City’s extensive monitoring in 2009.

Comment 34

D. Progress in Economic Development

The Draft Report criticizes the methods of past economic development programs and requests changes. Prior to the OIG audit, the City was already engaged in substantially changing its programs. While the audit criticizes the speed that this is occurring, please know, dissolving a public corporation is a complex process and corrective action must be taken comprehensively and carefully. The City has also developed a new program, not based on any template, but instead designed specifically to address the problems identified by the City with the previous loan program. Nonetheless, the City has made substantial progress to date.

The steps toward a new economic development program are in place and are proceeding. The general outline is as follows:

- | | | |
|-----|---|-------------|
| 1. | RFP for Economic Fund Manager: | Done |
| 2. | RFP for Technical Services Assistance: | Done |
| 3. | Scale back of former economic development subrecipient: | Done |
| 4. | Dissolution of that subrecipient, including final accounting
And distribution of assets: | In Progress |
| 5. | Identification of new Economic Fund Manager
and approval by the BURA Board | Done |
| 6. | Contract Negotiation with new Fund Manager: | In Progress |
| 7. | Identification of new tech services consultant: | In Progress |
| 8. | Receipt of commercial loan inquiries: | Ongoing |
| 9. | Establish new economic development loan program: | In Progress |
| 10. | Estimated Commencement of new program: | May, 2011 |

The City has formulated a clear plan and has begun to implement it. We have kept the Buffalo Field Office apprised throughout. The universal scale back of a main subrecipient and the concurrent ramp up of a new program is being entered into with effective planning and consultation. Action for the sake of action should not be encouraged or embraced.

Response to Finding Three

The City Worked with the Buffalo Field Office and Resolved Concerns Related to the Clean and Seal Program to Ensure Eligibility

Comment 35

The Buffalo Field Office issued Advisory Comments (dated August 26, 2009), for the 2009-2010 Annual Action Plan and advised that the Clean & Seal Program would only be eligible under the clearance activity if there was subsequent demolition of the property or the funds were used for purposes of code enforcement. The Buffalo Field Office advised the City to clarify whether the activity was tied to property demolitions, and if not, how it would meet another CDBG eligibility category. The City worked and continues to work closely with the Buffalo Field Office over the course of the year to insure proper qualification of this program.

The Buffalo Field Office staff advised the City that properties could only qualify if they were demolished within two (2) to three (3) years of the board up. After undertaking an analysis to

Comment 35

determine the approximate length of time to effectuate demolition of these properties, the City found that the majority of properties took five (5) years or more. At HUD's direction, the City reviewed alternative ways to qualify this essential program.

The City's proactive approach in the resolution of this matter resulted in the location of policy guidance in HUD's List of Memorandums entitled, "Boarding Up Buildings CDBG Entitlement Eligibility" dated May 14, 1990 (5/14/90 Memo). The City provided this memorandum to HUD and requested guidance.

The 5/14/90 Memo states:

Boarding up vacant buildings may also be classified as part of a code enforcement effort and along with other activities such as public improvements, rehabilitation and services which are expected to arrest the decline of the area.

See a full copy of this memorandum provided as **Exhibit K**.

The Buffalo Field Office agreed with the 5/14/90 Memo. Based upon that consensus, the City carried out an extensive analysis of identifying public improvements, rehabilitation and services for each board up address for 2009. The City identified 348 properties qualified under clearance, 830 properties qualified under Code Enforcement, and 57 properties qualified under rehab. In all cases the City maintains the board up activity met the community's needs because neighborhoods were being de-stabilized with unsecured structures increasing blight and becoming havens for criminal activity.

The HUD OIG should also be assured that all properties on the City's demolition lists are confirmed as to eligibility through on site inspections, which include photographic documentation and the finding to the contrary merits reconsideration. In addition, the finding concerning the addition of 300 properties to the City's demolition list misstates that 300 properties were added to the demolition lists (only 74 were added to the list upon site inspection).

Conclusion

The City concurs with HUD in that a thorough audit based upon all material information is essential to produce a document that accurately reflects a recipient's compliance with HUD Regulations and the CDBG Program Guidelines. As such, we appreciate this opportunity to provide facts that may be used to clear the City of many findings noted in the Draft Report.

We disagree with the findings related to street improvements and the clean and seal program. These findings merit removal as the information contained herein documents these as eligible activities. The finding related to the administration of the economic development subrecipient relationship merits reconsideration in light of the additional documentation provided herein, the progress the City has made to date in designing and implementing improvements in its economic development programming, and the corrective action taken as a result of BURA's monitoring.

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On behalf of the Mayor of the City of Buffalo, I thank you for this opportunity and request that you consider these written comments in any final report.

Thank you.

City of Buffalo

By: 

Janet Penksa Ph.D.

Commissioner of Administration, Finance, Policy and Urban Affairs

JP/rga

cc: Honorable Byron W. Brown, Mayor, City of Buffalo
Brendan R. Mehaffy, Vice Chairman, City of Buffalo Urban Renewal Agency
Karen A. Campbell, Assistant Regional Inspector General for Audit
William T. O'Connell, Director, Community Planning and Development Division

OIG Evaluation of Auditee Comments

- Comment 1** Officials for the City contend that OIG has reached subjective, and in some instances, unsupported conclusions. However, contrary to the officials' contention, the conclusions reached are fully supported by documentation requested and reviewed during the audit. Further, the results of the review were discussed throughout the course of the audit, and also at the meeting held on December 17, 2010 denoting the end of the onsite fieldwork, and at the exit conference. Thus, the contention of the officials is unwarranted.
- Comment 2** Officials for the City contend that the reorganization that the City has already performed is not fully recognized in the audit report. Although we recognize the corrective actions implemented by the officials, City officials have not made any organizational changes that would affect finding 1 or finding 3. In regard to finding 2 and the dissolution of the Buffalo Economic Renaissance Corporation (Corporation), the background section of the finding chronologically details the actions of the mayor to eliminate the Corporation and unify all of the neighborhood revitalization efforts under the Buffalo Urban Renewal Agency (Agency).
- Comment 3** Officials for the City contend that they were advised to limit their response to three pages per finding and that such a limitation doesn't allow for a full and fair review of the matters under review. However, City officials misinterpreted the auditors; at the exit conference, City officials were informed that their comments would be attached to the final report. It was fully explained that there were only three findings and that the Regional Inspector General for Audit (RIGA) reserves the right to summarize voluminous comments. It was further explained that sensitive or inappropriate information may also be redacted, and if that was to occur and explanatory statement would be included in the report as to why information was redacted.
- Comment 4** Officials for the City state that the report does not appear to adequately address the fact that there has been substantial operating and staff changes, including the removal of prior administrators, and the dissolution of the City's primary economic development agent (Corporation). As noted in the report, the audit scope covered the period May 1, 2008, through April 30, 2010, and was extended as necessary. The audit disclosed issues in the City's administration of its CDBG program during this time period, regardless of administrators in place. Regarding the dissolution of the Corporation, as stated above in comment 2, the background section of finding 2 chronologically details the dissolution.
- Comment 5** Officials for the City assert that its review of the Corporation's dissolution is ongoing, comprehensive, and methodical, and that they are committed to assuring compliance with HUD regulations. However, at no time during or after the audit were we provided with any evidence of such a review. Nevertheless, if such a

review was indeed performed by the City, it does not supersede HUD requirements of the Agency (BURA) to monitor the Corporation (BERC).

- Comment 6** Officials for the City submitted exhibits referenced in their response under separate cover. We reviewed the additional documentation and exhibits submitted subsequent to the audit and determined that they still do not adequately support the deficiencies identified. Refer to the applicable comments below.
- Comment 7** Officials for the City request reconsideration for finding 1, citing that all of the street improvements questioned were associated with eligible areas, including those claimed to be located in substantially industrial or non-low income census tracts. However, the street improvements in question were not deemed only ineligible because they are located in substantially industrial or non-low income census tracts, but also because the expense was charged against the CDBG program in order to meet HUD's 1.5 timeliness test for 2009. Specifically, the City reimbursed previously incurred general City maintenance expenses in order to expend CDBG funds quickly to prevent a reduction in future funding. Further, the street improvements in question were found to be unsupported because the City did not maintain, at the time the expenditures were incurred going back as far as June 2007, documents that showed that the expenditures met a national objective and had a community benefit.
- Comment 8** Officials for the City contend that the City is an older industrial city, thus the street improvements should be reconsidered as part of their efforts to make the streets safe. We recognize the fact that the City, along with many other cities throughout the country, faces such dilemmas in an ever-changing landscape. However, in accordance with HUD regulations, such public improvement expenditures must be the most efficient and economical use of CDBG funds, benefitting persons of low and moderate income based on community needs. The City was unable to provide evidence of how the CDBG eligibility criteria were met.
- Comment 9** Officials for the City request that the draft audit recommendations related to the monitoring of the Corporation (BERC) be reconsidered based on the substantial corrective action initiated prior to the audit fieldwork. However, during the audit the officials were unable to provide evidence of monitoring its subrecipient administered economic development program.
- Comment 10** Officials for the City acknowledge that they were made aware of the reported deficiencies during a pre-exit conference held on December 20, 2010, but believed that we did not consider the additional information that they provided. We considered the additional documentation provided by the officials subsequent to the pre-exit conference only in the context of the audit scope when preparing the draft audit report. Nevertheless, the reportable deficiencies remained unchanged.

- Comment 11** Officials for the City state that the activities of the Corporation (BERC) were actively monitored in 2008 and 2009, and based on this monitoring, officials decided to end its subrecipient agreement with the Corporation (BERC) in February 2010. However, at the time of our review, officials were unable to provide evidence of such monitoring. Further, the review performed by the officials regarding the dissolution of the Corporation (BERC) does not supersede the HUD requirements for the Agency (BURA) to monitor the Corporation (BERC).
- Comment 12** Officials for the City contend that all of the Corporation's (BERC's) program income was returned to the City and they provided supporting evidence of such action. We have reviewed the documentation and determined that the returning of program income was subsequent to our audit period, and thus does not negate the significant concerns identified in the finding, which occurred prior to the commencement of the dissolution process.
- Comment 13** Officials for the City contend they have maintained sufficient documentation as evidence of the eligibility of its clean and seal program activities in accordance with federal regulations, which provide that the boarding up of vacant buildings may be classified as code enforcement. However, the officials need to further recognize that the guidance also provides that the boarding up must be carried out as part of a code enforcement effort along with other activities such as public improvements, rehabilitation, and services which are expected to arrest the decline of the area. The audit work determined that the board up was not accompanied with the other activities, i.e. public improvements, as identified in the guidance. In addition, it was determined that the code enforcement expenditures were for the cost of correcting code violations, which is contrary to HUD regulations.
- Comment 14** Officials for the City state that the conclusions in the draft report are premature in light of the volume of data not considered during the audit. As a courtesy, we allowed the City to submit additional documentation subsequent to the completion of the audit fieldwork. We reviewed the additional documentation, some of which was the same documentation reviewed onsite, and determined that it still did not adequately support the reportable deficiencies identified. Thus, the conclusions reached in the draft report are fully supported based on the documentation reviewed onsite and subsequent to the fieldwork, and therefore, are not premature. Nevertheless, we have taken into consideration HUD's comments on the draft report and have revised the last sentence in the "What We Found" section of the report to reflect that the City was not able to demonstrate that it made the best use of CDBG funds to meet the community's needs.
- Comment 15** Officials for the City disagree that the BURA (Agency) paid for the same work twice on Courtland Avenue based on the fact that Courtland Avenue lies on the border of two districts and the cost of the repaving work was apportioned between the two districts. However, although the street appears to lie on the border of two

districts, the documentation provided by the officials subsequent to the audit (Exhibit B) does not support the apportionment between the districts. Thus, it cannot be determined how much this particular street project cost in relation to the two districts based on the source contractor invoices. Further, one of the districts reimbursed the City \$28,680 from CDBG funds, while the other district reimbursed \$28,211, nevertheless, the documentation provided also does not support how or why the east half of the street would cost more than the west half, considering both halves are equal in length.

Comment 16 Officials for the City concede that a typographical error was made on the support provided which indicated West Parade Avenue was repaved from Northampton Street to East North Street. Our review of documentation maintained by the BURA (Agency) detailed that the City was reimbursed \$14,982 for work performed only on the section from Best Street to East North Street. The officials admit that an error was made and that the reimbursement was for mill and overlay work on West Parade Avenue from the Kensington Expressway to Best Street. However, the fact remains that the section of West Parade Avenue reimbursed with CDBG funds was not repaved as indicated by the support maintained by the BURA (Agency). Further, it could not be determined from the support maintained by the City's Department of Public Works (DPW) as to what section of the West Parade Avenue was to be reimbursed from CDBG funds and what section was not. Since the amount of \$14,513 paid by the City could not be traced to the contractors' invoiced amount, it is still considered unsupported.

Comment 17 Officials for the City again concede that another error had occurred, whereby Academy Road was inadvertently included in a list of projects deemed to be completed. Officials claim that the CDBG funds for the Academy Road curb replacement project were withheld until the work was completed and that the \$114,000 has been fully repaid to the BURA (Agency). To prevent such errors from occurring in the future, officials have revised its policy manuals to require photographic evidence of all physical development projects prior to payment. The corrective actions taken by the officials are responsive to our finding and do not negate the fact that the City disbursed \$114,000 in CDBG program funds for work that was not performed. Accordingly, this deficiency is reportable.

Comment 18 Officials for the City disagree that the street improvements on Urban and Amherst Streets only primarily benefit an industrial area, and object to the use of photographs used to support that premise. Contrary to the officials' disagreement, the street repaving projects are questionable since a factory occupies Urban Street and a railroad viaduct occupies Amherst Street. The photographs of the factory on Urban Street and the vacant land and railroad tracks on Amherst Street calls into question how street improvements in these areas met HUD's primarily residential criteria in accordance with regulations at 24 CFR 570.208(a). For example, while 40 percent of Urban Street consists of private residences and a school, the remaining 60 percent is non-residential, consisting of several factories and other industrial-use sites. According to 24 CFR 570.208, an area that is not

primarily residential in character does not qualify to meet the area-wide CDBG national objective of benefiting low- and moderate- income persons. Although we have removed the photographs in question from the draft report, we are still questioning the City's basis for determining the area served by certain street improvement projects, and recommend submission of information to support their service area determination and why these costs were not charged as general City maintenance expenses instead of CDBG expenses.

Comment 19 Officials for the City provided census data to support that the street improvements on West Ferry Street benefitted low- and moderate- income persons. However, the benefit of the improvements is not the point of contention. The process of how improvement projects are selected amongst the City's nine districts is questionable. Rather than use CDBG funding based on the City's overall infrastructure needs, officials distributed the CDBG funds equally among the City's nine districts without any corresponding method or basis. Thus, it is questionable as to whether the expenditures were the most efficient and economical use of CDBG funds.

Comment 20 Officials for the City state that its consolidated plan lists infrastructure improvements as a high priority need and provides for use of CDBG funding for street and sidewalk improvements in low and moderate income areas of the City. Officials contend that street improvements were bid out and then reimbursed by the CDBG program to obtain greater economies of scale. The reimbursement method is the City's preferred method for expending CDBG funds in compliance with HUD regulations. However, the reimbursements for the CDBG expenditures reviewed during the audit were for City expenses incurred as far back as June 2007. In addition, at the time the expenditures were incurred, the City did not maintain documentation to support that the expenditures met a national objective and had a community benefit. Thus, the corrective action taken by the City to change its policy manual to include photographic documentation and onsite monitoring before reimbursement of any future work is responsive to our finding and recommendation.

Comment 21 Officials for the City state that construction contracts are bid through a formal bidding procedure and that all records and personnel related to procurement were made available during the review. Further, the officials detail how public improvements funded by the CDBG program will be bid out in the future. We reviewed documentation onsite during the audit and the documentation provided by City officials subsequent to the audit (Exhibit J), and determined that sufficient records were not maintained to support the procurement history for the street improvement projects reviewed. While we recognize that the policy changes pertaining to the future bidding process is responsive to our finding, the changes do not negate the procurement weaknesses identified. Thus, the eligibility of the more than \$1.9 million in costs remains unsupported, pending further review by HUD as recommended.

Comment 22 Officials for the City contend that that during the audit access to all records necessary to review alleged unsupported transactions was provided. Officials request that the draft report reflect this fact. During the audit, we reviewed and considered the records and documentation provided in relation to the context of the audit scope as explained in the Scope and Methodology section of the report. As a courtesy, we allowed the City to submit additional documentation subsequent to the completion of the audit fieldwork. We reviewed the additional documentation, some of which was the same documentation reviewed onsite, and determined that it still did not adequately support the reportable deficiencies identified. Thus, the draft report stands.

Comment 23 Officials for the City request that the draft report reflect that for 2008 the BURA (Agency) and the BERC (Corporation) operated as one entity through its common CFO and access to the Laser fiche document scanning system, therefore any findings pertaining to the lack of records maintained by the BURA (Agency) should be removed. Regardless of the systems implemented by the City, the relationship between the BURA (Agency) and the BERC (Corporation) was contractual. Further, it was determined that unsupported program income amounts were reported to HUD and that questionable transactions were charged to the CDBG program income account as identified in finding 2. Thus, since the documentation provided did not negate the identified concerns, the findings remain as detailed in the draft report.

Comment 24 Officials for the City request that the draft report acknowledge its reorganization and separation of the BURA (Agency) and BERC (Corporation) administrations in July 2009 and the end of the City's subrecipient relationship with the BERC (Corporation) in February 2010. The background section of finding 2 in the draft report chronologically details the actions of the mayor to eliminate the BERC (Corporation) and unify all of the neighborhood revitalization efforts under the BURA (Agency). Nevertheless, as mentioned above, since the documents provided by the City did not negate the identified concerns, finding 2 will not be removed.

Comment 25 Officials for the City disagree that \$4.9 million of economic development program income and receipts were unsupported. Contrary to the disagreement by the officials, we reviewed all documentation provided and determined that the City did not obtain adequate documentation supporting that program income had been properly recorded. Specifically, as detailed in finding 2, (1) information submitted by the BERC (Corporation) to the City consisted merely of a spreadsheet with no supporting documents, (2) the City included rental receipts after the deduction of rental expenses without support, (3) expenditures related to payroll and operations were unsupported, and (4) the BERC (Corporation) submitted a number of invoices in which the documentation did not support how the cost was allowable. Even the CDBG program manager agreed during the audit that certain expenditures, such as legal fees and expenditures after the fiscal year should not have been charged to the CDBG program during fiscal year 2009.

The concerns identified in the report support the conclusion that the BURA (Agency) did not provide sufficient evidence that they reviewed the documentation or assessed the validity of documentation prior to reimbursement with CDBG program funds.

Comment 26 Official for the City state that the BERC (Corporation) is now required to provide the BURA (Agency) copies of necessary documentation. Thus, the actions taken by the officials are responsive to our finding and are in concurrence with our results that the necessary documentation was not provided by the BERC (Corporation) to the BURA (Agency).

Comment 27 Officials for the City request that the finding pertaining to payroll be removed since access to payroll records which supports the expenditures was provided. Hence, we reviewed and considered the payroll records referred to in the context of the audit scope during the review, and although many documents were provided, they were not relevant to the audit objective. Thus, the BURA (Agency) did not provide evidence that they reviewed the documentation or assessed its validity.

Comment 28 Officials for the City indicate that the BERC (Corporation) provided reimbursement from non-federal funds an amount paid to a former employee for accrued time owed at the time of separation. The officials acknowledge that some amounts were to be returned to the BURA (Agency). Thus, the actions taken by the officials, although pertaining to transactions subsequent to our audit period, are responsive to our finding and recommendations.

Comment 29 Officials for the City request that the questionable eligibility pertaining to other invoices be reconsidered. Based on the scope of the audit, these additional invoices were reviewed during and subsequent to the audit and found to be insufficient; therefore, these items are still questionable.

Comment 30 Officials for the City contend that the methodology used by the auditors to arrive at a total of \$4.9 million in reported economic development program income is unsupported and based on the unconventional method of combining both debits and credits. The methodology followed takes into consideration both program income receipts and program income expenditures as reported to HUD. HUD regulations require subrecipients to ensure that both program income receipts and expenditures are in accordance with program requirements, and since the documentation provided was not sufficient to support these items; the City's exposure is \$4.9 million in transactions pertaining to its economic development program.

Comment 31 Officials for the City disagree with the finding that the BERC (Corporation) recorded more than \$15.2 million in questionable transactions in its CDBG program income account. While the officials' disagreement is noted, the fact remains that we reviewed all documentation provided and considered such

documentation in the context of the audit scope prior to preparing the draft report. The concerns identified in the report are factual and the conclusions are supported. We are questioning both program income receipts recorded and program income expenditures paid during fiscal years 2008 and 2009. HUD regulations require the City to provide assurance that all CDBG program income receipts were recorded and expenditures were eligible to be paid with program income funds. As mentioned above, since the information provided was not sufficient to answer our concerns, these items have been questioned and now require further review and explanation to HUD.

Comment 32 Officials for the City state that additional information was provided subsequent to the audit regarding the funding source of the unsupported transactions and other supplemental information. As mentioned earlier, all documentation provided during and subsequent to the audit fieldwork was reviewed, and found to be insufficient for the removal of the issues from this report.

Comment 33 Officials for the City state that corrective actions were taken to safeguard the assets in control of the BERC (Corporation) and that the report fails to recognize the mayor's reorganization of its economic development programs, that were the result of extensive monitoring in 2009. However, actions taken by the officials were subsequent to the audit and did not safeguard the assets reviewed as part of the audit scope from May 1, 2008 through April 30, 2010, and extended as necessary. Further, officials did not provide documented evidence of the monitoring that supposedly occurred in 2009 (i.e. monitoring reports, etc.). Nevertheless, the review performed by the City regarding the dissolution of the BERC (Corporation) does not supersede HUD requirements of the BURA (Agency) to document its monitoring of the BERC (Corporation).

Comment 34 Officials for the City contend that a clear plan toward implementing a new economic development program has begun. However, while the City attempts to reorganize, it continues to have more than \$4.7 million dollars in economic development funds not being used for its intended purposes.

Comment 35 Officials for the City provide details on their working relationship with the HUD Buffalo Field Office in order to resolve concerns relating to the clean and seal program. The officials provide a May 14, 1990 memorandum to support the questioned clean and seal program costs. While this guidance indicates that boarding up vacant buildings may be classified as code enforcement, it also states that the boarding up must be carried out along with other activities such as public improvements, rehabilitation, and services which are expected to arrest the decline of the area. However, the results of the audit determined that the board up was not accompanied with the other activities, i.e. public improvements, as identified in the guidance.