



Issue Date December 8, 2008
--------------------------------

Audit Report Number 2009-NY-1004
-------------------------------------

TO: Kathleen Naymola, Director, Community Planning and Development, 2FD

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

SUBJECT: The Economic Development Corporation Did Not Administer Its Community Development Block Grant Program in Accordance with HUD Requirements

## **HIGHLIGHTS**

### **What We Audited and Why**

We audited the Community Development Block Grant (CDBG) program administered by the Economic Development Corporation (Corporation), a subgrantee of Essex County Consortium (the County). We selected the Corporation for review because our audit of the County's CDBG operations disclosed that the County did not have adequate controls over this subgrantee to ensure its compliance with U.S. Department of Housing and Urban Development (HUD) requirements. Also, HUD's risk analysis indicated that the Corporation had excessive loan amounts and little activity. Our audit objectives were to determine whether the Corporation adequately administered its CDBG program in accordance with applicable rules and regulations. Specifically, we wanted to determine whether it efficiently and effectively disbursed CDBG funds, had a financial management system in place to adequately safeguard the funds, and used CDBG funds to meet the national objectives.

### **What We Found**

The Corporation did not adequately administer its CDBG program. Specifically, it (1) did not properly administer economic development loan programs, (2) improperly converted a loan to a grant and received a duplicate drawdown, (3) did not carry out adequate technical assistance and site search services, (4) could not support that its activities met the CDBG national objectives, and (5) lacked evidence

to justify its CDBG administrative expenses. This noncompliance occurred because the Corporation did not develop and implement policies and procedures to ensure its compliance with HUD's requirements. As a result, more than \$660,000 of the revolving funds was not effectively used to make economic development loans, \$133,000 was ineligibly drawn down for economic development loans, and more than \$1.6 million disbursed for administrative expenses was not justified.

Also, the Corporation did not always comply with HUD requirements to ensure that (1) adequate financial records were maintained for its two economic development loan programs, (2) program income was properly accounted for, and (3) adequate budget and cost allocation procedures were implemented. As a result, financial records were inadequately maintained; program income was improperly recorded; and CDBG funds were not properly budgeted, allocated, and safeguarded.

### **What We Recommend**

We recommend that the Director of HUD's New Jersey Office of Community Planning and Development instruct the County to require the Corporation to (1) develop and implement appropriate program plans and controls to ensure that \$662,184 in CDBG funds is used effectively to make economic development loans, (2) repay \$100,000 for the ineligible loan and \$33,000 for the duplicate drawdown, (3) obtain and submit all supporting documentation showing the appropriateness and eligibility of more than \$1.6 million in administrative expenditures, (4) develop and implement proper financial controls to safeguard CDBG funds, and (5) establish adequate procedures to ensure that receipts and expenditures of program income are properly recorded and reported. We also recommend that the County discontinue further funding to the Corporation until HUD determines that it has the capacity to carry out CDBG 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 provided a draft report to auditee officials on September 23, 2008, and requested their responses by October 14, 2008. We discussed the results of our review during the audit and at an exit conference held on October 14, 2008, on which auditee officials provided their written comments. Auditee officials generally disagree with the draft report findings. The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report. The auditee provided numerous exhibits at the exit conference and a more detailed response subsequent to the exit conference that were too large to be included in this report, but which will be provided to the Field Office for review.

# TABLE OF CONTENTS

---

Background and Objectives	4
Results of Audit	
Finding 1: The Corporation Inadequately Administered Its CDBG Program	5
Finding 2: There Were Control Weaknesses in the Corporation’s Financial Management System	10
Scope and Methodology	14
Internal Controls	15
Appendixes	
A. Schedule of Questioned Costs and Funds to Be Put to Better Use	17
B. Auditee Comments and OIG’s Evaluation	18

## 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). 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 of the community.

The Economic Development Corporation (Corporation), is a private nonprofit organization and is a subgrantee of the Essex County Consortium (County). The Corporation was incorporated in November 1982 to promote the economic growth in Essex County and has received annual CDBG funds to carry out economic development programs for the County. During program years 1999 to 2006, the Corporation disbursed approximately \$1.7 million in CDBG funds to administer its economic development activities including two CDBG-financed revolving loan programs—Community Development Revolving Loan Fund (CDRLF) and Community Economic Revitalization Program (CERP). Both of these programs were to provide financial assistance to local businesses to either create job opportunities or benefit the area through facade improvements. In addition, CDBG administrative funds were used to cover the overhead of other non-CDBG-financed economic development loan programs and consulting services such as technical assistance and site search services.

Currently, the Corporation only has one full-time employee and a part-time executive director who also serves as the director of the County's Office of Small Business and Affirmative Action. The Corporation is located at the County's Hall of Records, 465 Dr. Martin Luther King, Jr., Boulevard, Newark, New Jersey.

We audited the Corporation because our audit of the County's CDBG operations disclosed that the County did not have adequate controls over this subgrantee to ensure its compliance with U.S. Department of Housing and Urban Development (HUD) requirements. Also, a HUD risk analysis indicated that the Corporation had excessive loan amounts and little activity. Our audit objectives were to determine whether the Corporation adequately administered its CDBG program in accordance with applicable rules and regulations. Specifically, we wanted to determine whether it efficiently and effectively disbursed CDBG funds, had a financial management system in place to adequately safeguard the funds, and used CDBG funds to meet the national objectives.

## RESULTS OF AUDIT

---

### Finding 1: The Corporation Inadequately Administered Its CDBG Program

The Corporation did not adequately administer its CDBG program. Specifically, it (1) did not properly administer economic development loan programs, (2) improperly converted a loan to a grant and received a duplicate drawdown, (3) did not carry out adequate technical assistance and site search services, (4) could not support that its activities met the CDBG national objectives, and (5) lacked evidence to justify its CDBG administrative expenses. This noncompliance occurred because the Corporation did not develop and implement policies and procedures to ensure its compliance with HUD's requirements, and the County did not have proper program and financial controls over the CDBG activities administered by the Corporation. As a result, more than \$660,000 in revolving funds was not effectively used to make economic development loans, \$133,000 was ineligibly drawn down for economic development loans, and more than \$1.6 million in administrative expenses was not justified or reasonable.

---

#### **Economic Development Loan Programs Not Administered Properly**

The Corporation did not properly administer its CDBG economic development revolving loan program. Specifically, it lacked productivity in making CDBG economic development loans and did not follow HUD regulations in originating and administering an economic development loan of \$100,000 through the Community Development Revolving Loan Fund (CDRLF) program in 2005. As a subrecipient of the County's CDBG entitlement grant since the mid-1980s, the Corporation had administered the County's CDBG economic development loans through the CDRLF program, which was supposed to help to create jobs, and the Community Economic Revitalization Program (CERP), which was supposed to result in facade improvements and area benefits. The Corporation used the proceeds from loan repayments to generate new economic development loans and used the annual CDBG grant from the County to pay for administrative expenditures of these activities.

The annual performance reports submitted by the Corporation to HUD demonstrated that the Corporation was passive in making economic development loans and lacked productivity in originating loans. Except for two CDRLF loans, which were made in August and November 2005, the Corporation had not generated any CDRLF loans since September 1995. In addition, one of the two CDRLF loans had defaulted and was improperly converted to a grant because it had not complied with the subrecipient agreement and job creation objectives (see the "Improper Loan Conversion and Drawdown" section). Further, only one CERP loan had been

originated since program year 1999. Therefore, the Corporation did not use CDBG funds in a timely manner and diminished the objectives and accomplishments of the CDBG program. These two revolving loan funds had balances of \$326,852 (as of September 13, 2007) and \$335,332 (as of August 31, 2007), respectively. Corporation staff acknowledged the slow progress and stated that they could have done better. Moreover, there was little evidence that the CDRLF loans achieved job creation objectives during program years 1999 to 2006 (see the “Unsupported Accomplishment of National Objectives” section).

Accordingly, the Corporation did not comply with the regulations at 24 CFR (*Code of Federal Regulations*) 85.20(a) (4) and 570.200 (a)(3) pertaining to performance and productivity of HUD programs. As a result, there was no assurance that more than \$660,000 in remaining revolving loan funds would be used effectively as funds had not been used to make loans to businesses, create jobs, or make other improvements.

### **Improper Loan Conversion and Drawdown**

The Corporation did not follow HUD regulations in originating and administering an economic development loan of \$100,000 through the CDRLF program in 2005. Regulations at 24 CFR 570.209 provide that a recipient who used CDBG funds for special economic development activities must create or retain at least one full-time equivalent permanent job per \$35,000 in CDBG funds used. The loan agreement indicated that the loan proceeds would be used for the construction of a day care business to benefit students from low- and moderate-income families and that the borrower must meet the job creation and day care student enrollment objectives. In addition, the loan could be converted to a CDBG grant if the borrower met these two objectives. However, instead of declaring default and taking remediation actions, the Corporation improperly converted the loan to a grant, although the borrower did not achieve the job creation objectives. This fact was corroborated by the independent public accountant’s audit report of the Corporation, which provided that the loan recipient failed to comply with the job creation requirements. Further, the loan was awarded without adequate collateral or proper analysis of the borrower’s solvency, and the grant agreement between the Corporation and the County did not authorize the Corporation to provide grants to local businesses. The loan agreement did not require collateral, and correspondence from the bank and the recipient confirmed that there was no collateral to secure the loan. Moreover, awarding grants by using CDRLF was not in compliance with the objectives of this program. Therefore, this CDRLF loan was ineligible, and the \$100,000 should be reimbursed to the CDBG program from nonfederal funds.

In addition, the Corporation received a duplicate drawdown of \$33,000 from the County for a CDRLF loan due to an error. This amount should also be reimbursed to the CDBG program from the Corporation’s CDRLF bank account.

### **Inadequate Technical Assistance and Site Search**

According to the annual action plan submitted to HUD through the County, the Corporation provides technical assistance and site search services to local businesses. The Corporation's application for the CDBG grant specified that the assistance would include assisting businesses in preparing business plans that were designed to support the growth of area business and job opportunities, as well as educating and supporting small businesses in Essex County through conferences and meetings. Several Corporation employees charged their time to technical assistance services over the years. However, the Corporation only assisted 7 of 161 local businesses that sought assistance in preparing business plans during program years 1999 to 2006. Only two of the seven assisted businesses received CDBG-financed loans from the Corporation. The remaining 154 businesses were not given adequate attention or assistance.

The Corporation's application further described that the Corporation would provide site search services to local businesses seeking areas to relocate, start up, or expand within Essex County. However, it did not deliver site search services before program year 2004 and only performed limited site search services after program year 2004.

As a result of the ineffective technical assistance and site search services, the Corporation could not generate sufficient economic development loans to help local businesses or meet job creation objectives.

### **Unsupported Accomplishment of National Objectives**

The Corporation did not maintain adequate documents to demonstrate that it met at least one of the three CDBG national objectives as prescribed by 24 CFR 570.200. Regulations at 24 CFR 209 provide that a recipient who used CDBG funds for special economic development activities must create or retain at least one full-time equivalent permanent job per \$35,000 in CDBG funds used for economic development projects. The annual performance report submitted to HUD by the Corporation claimed that the majority of economic development loans it originated met the national objective of benefiting low- and moderate-income persons. However, the loan agreement between the Corporation and the businesses indicated the number of jobs to be created but did not provide the titles of these jobs. The supporting documentation for accomplishments only showed the list of new employees; therefore, the Corporation could not show whether the reported jobs were created or refilled. In addition, the list of new employees could not adequately support that the number of jobs was counted accurately



because more than one employee could have been hired for a same position during a program year.

Further, multiple technical assistance loans did not achieve job creation objectives. The loans were financed by non-CDBG funds, and their administrative costs were paid with CDBG funds. Although the loans were closed more than five years ago, no jobs had been created. However, instead of enforcing HUD regulations and taking appropriate corrective actions against the loan recipients that failed to accomplish job creation objectives in a timely manner, the Corporation stated in its annual performance report that it was still in the process of collecting job creation data for these loans. Therefore, it did not effectively monitor the job creation results of its loan recipients.

As a result, the Corporation did not properly evaluate the jobs created during these years and ensure compliance with HUD regulations and the national objectives.

### **Unsupported/Ineligible Administrative Costs**

The Corporation disbursed more than \$1.6 million for administrative costs during program years 1999 through 2006 to manage the economic development loans, provide technical assistance and site search services to local businesses, and ensure accomplishment of the national objective of job creation. However, these administrative costs did not appear to be reasonable. The Corporation only generated three CDBG-financed loans, provided technical assistance to seven businesses, and carried out limited site search services for business. In addition, it did not maintain adequate documents to demonstrate that its activities met the CDBG national objective of job creation. As a result, it lacked evidence to support that it administered its CDBG activities in accordance with federal regulations and its action plan submitted to HUD. Since the Corporation did not carry out its economic development loan programs, technical assistance, and site search services, as stated in its action plan and submission to HUD, or achieve the objectives of increasing business growth and creating jobs, the administrative costs for these activities are questioned pending an eligibility determination by HUD.



## Conclusion

The Corporation did not adequately administer its CDBG programs. Consequently, more than \$660,000 in revolving funds was not used effectively to make economic development loans, CDBG funds were not safeguarded as \$133,000 was ineligibly drawn down for economic development loans, and more than \$1.6 million in administrative funds was disbursed without adequate support that the costs were reasonable and eligible. This noncompliance occurred because the Corporation did not develop and implement policies and procedures to ensure its compliance with HUD's requirements, and the County did not have proper program controls over the CDBG activities administered by the Corporation.

## Recommendations

We recommend that the Director of HUD's New Jersey Office of Community Planning and Development instruct the County to

- 1A. Require the Corporation to develop and implement an adequate program plan and proper management controls to ensure that \$662,184 or the current balance of CDBG funds in the two revolving loan accounts is used to make economic development loans, thus ensuring that these funds are put to better use.
- 1B. Require the Corporation to develop and implement appropriate review and monitoring procedures to minimize the risk of defaulted loans.
- 1C. Require the Corporation to reimburse \$100,000 from nonfederal funds to the CDBG program for the ineligible loan and \$33,000 from its CDRLF bank account to the CDBG program for the duplicate drawdown.
- 1D. Require the Corporation to obtain and submit all supporting documentation for the CDBG activities carried out and the jobs created during program years 1999 to 2006 so that HUD can determine compliance with HUD regulations and the eligibility and reasonableness of the \$1,678,332 that the Corporation disbursed for administering its CDBG economic development activities during that period. Any amounts determined to be ineligible or unreasonable must be reimbursed to the CDBG program from nonfederal funds.
- 1E. Discontinue funding the Corporation with CDBG funds until HUD determines that it has the capacity to carry out CDBG economic development activities in compliance with HUD regulations.

## Finding 2: There Were Control Weaknesses in the Corporation's Financial Management System

The Corporation had weaknesses in its financial management system. Specifically, it did not always comply with HUD requirements to ensure that (1) adequate financial records were maintained for its two economic development loan programs, (2) program income was properly accounted for, and (3) adequate budget and cost allocation procedures were implemented. This noncompliance occurred because the Corporation did not develop and implement adequate procedures to ensure compliance with HUD requirements. As a result, financial records were inadequately maintained, program income was improperly recorded, and CDBG funds were not properly allocated and safeguarded.

---

### Inadequate Financial Records

The County issued a monitoring report regarding the Corporation's noncompliance with its financial and management controls in program year 2005. Our review confirmed that the Corporation lacked financial controls for its CDBG programs and that no corrective actions were taken in response to the County's monitoring review.

Regulations at 24 CFR 85.42, 570.506, and 570.502 indicate that the grantee should maintain proper supporting documentation for at least four years after the last expenditure report is submitted, in which the activity is reported as complete. The Corporation did not maintain adequate records such as the original grant agreements or the history of the grants for its two economic development loan programs: the Community Development Revolving Loan Fund (CDRLF) and the Community Economic Revitalization Program (CERP). The documentation provided only indicated that there had been a lump-sum drawdown of \$700,000 from CDBG funds related to the CDRLF program. However, the current Corporation staff stated that they only received \$453,742 of the \$700,000 and accumulated the current balance from the repayments of CDRLF loans. According to the Corporation, \$257,383 in CDRLF initial funding was reprogrammed to the County's other CDBG activities in 1991. In addition, the Corporation stated that it did not receive initial start-up funding from CDBG for its CERP loan program. However, these explanations were not supported by adequate documents; therefore, the Corporation could not show that the information regarding the initial funding, financial transactions, and current balances for these two revolving loan programs was accurate. Moreover, because of its inadequate financial records, HUD and the citizens of Essex County were not adequately notified of all major changes to the Corporation's CDBG activities.

### **Inadequate Accounting for Program Income**

The Corporation did not properly record loan repayments and improperly transferred funds between CDBG-financed and non-CDBG-financed programs. This conduct violated regulations at 24 CFR 570.200, which require that an activity may be assisted with CDBG funds only if it meets one of the CDBG national objectives. For example, the Corporation's general ledger disclosed that the monthly repayments of a CDRLF loan were not deposited into the CDRLF account; instead, they were deposited into the non-CDBG-financed revolving loan fund account. In addition, although the Corporation transferred a lump-sum amount back to the CDRLF account four years later, the total repayment amount of this loan to the CDRLF account was approximately \$1,900 less than the loan principal amount. Moreover, there were at least four other loans for which repayments were deposited into the revolving loan fund account for several months; however, the Corporation only transferred the principal amount back to the CDRLF account. As a result, program income, including the interest earned from these four CDRLF loans, was not fully returned to the CDRLF account and might have been used for non-CDBG activities. Therefore, the CDBG funds were not properly safeguarded.

Regulations at 24 CFR 85.20, 24 CFR 570.504, and 570.500 require that receipts and expenditures of program income be recorded as part of the financial transactions of the grant program and are subject to all applicable requirements governing the use of CDBG funds as mentioned above. The Corporation obtained repayments of principal and interest on economic development loans and also charged late fees to borrowers that did not repay loans on time. During program years 2004 to 2006, these repayments and late fees were deposited into the economic development loan accounts and used to finance other loans. However, the Corporation did not adequately report the income generated by these transactions to the County or HUD. The total amount of program income was \$68,820 for these three program years. Therefore, the County and HUD were not provided a proper accounting for the program income related to the CDBG economic development loan programs administered by the Corporation.

### **Inadequate Budget and Cost Allocation Plan**

The Corporation did not have an adequate budget for CDBG activities. Regulations at 24 CFR 85.20(b)(4) require that grantees' financial information be related to performance or productivity data, including the development of unit cost information. However, the grant agreement between the County and the Corporation did not provide a breakdown of budget information for individual economic development activities, except for the lump-sum amount of the CDBG funds awarded to the Corporation. Accordingly, the Corporation did not indicate how its CDBG and other funds were going to be budgeted among its loan

programs and economic development activities such as site search and technical assistance. As a result, due to the lack of a budget by type of activity, it was difficult for the County and HUD to evaluate the performance against the funds provided for each activity.

In addition, there was no evidence showing that the Corporation allocated the administrative costs among CDBG activities and non-CDBG activities in accordance with the regulations in Office of Management and Budget Circular A-87. Documentation submitted by the Corporation to the County for its administrative cost reimbursements indicated that its CDBG administrative costs were categorized into “salaries” and “expenses.” However, salaries and expenses were not associated with the CDBG activities that the Corporation was supposed to carry out as suggested in its action plan submitted to HUD. It carried out not only CDBG activities, but also non-CDBG activities. For example, the financial statement indicated that the Corporation incurred \$180,000 in CDBG expenses and more than \$1.5 million in non-CDBG expenses for program year 2005. However, it did not have a proper cost allocation plan to prorate the salaries and overhead costs between CDBG activities and non-CDBG activities. Corporation staff stated that the cost allocation ratio was determined by the Corporation’s executive director and fiscal analyst/program monitor; however, this ratio was not approved by the County or HUD. As a result, CDBG funds may have been used on non-CDBG-related activities and, therefore, may have been ineligible.

## **Conclusion**

The Corporation had weaknesses in its financial controls. For instance, financial records were inadequately maintained, program income was inadequately accounted for, and there were inadequate budget and allocation procedures. As a result, the Corporation could not show that the information regarding the initial funding, financial transactions, and current balances for its two revolving loan programs was accurate; program income consisting of the interest earned from loans was not fully returned to the CDRLF account; and CDBG sources and uses of funds may not have been accurately allocated to activities and may have been used for non-CDBG-related expenses. This condition resulted from the Corporation’s not establishing and implementing adequate financial controls.

## Recommendations

We recommend that the Director of HUD's New Jersey Office of Community Planning and Development instruct the County to

- 2A. Require the Corporation to develop and implement adequate controls to ensure proper record keeping for its CDBG activities.
- 2B. Require the Corporation to obtain and submit all supporting documentation for the disbursements from and deposits into its economic development loan accounts (the CDRLF and CERP programs) so that HUD can assess the correct balances for these programs. Any amounts determined to be ineligible must be reimbursed to CDBG program from nonfederal funds.
- 2C. Require the Corporation to develop and implement adequate controls to ensure that receipts and expenditures of program income are properly recorded and reported.
- 2D. Require the Corporation to develop and implement an adequate budget processing and cost allocation plan to ensure that CDBG funds and expenditures are properly allocated to individual activities.

## SCOPE AND METHODOLOGY

---

The audit focused on determining whether the Corporation administered its CDBG programs in accordance with HUD requirements. To accomplish our objectives, we

- Reviewed relevant federal and New Jersey state regulations;
- Interviewed appropriate personnel of HUD's Office of Community Planning and Development, Newark field office, and reviewed relevant grant files to obtain an understanding of CDBG program requirements and identify HUD's concerns with the County's operations;
- Reviewed the Corporation's policies, procedures, and practices and interviewed key personnel to obtain an understanding of its administration of the CDBG program;
- Reviewed monitoring reports and independent accountant audit reports; and
- Reviewed and tested the Corporation's files and records of selected activities to determine whether the costs were eligible and adequately supported as required by HUD regulations.

The Corporation had only generated two CDRLF loans since September 1995 and one CERP loan since June 1999. We reviewed all three of the loans. Since the Corporation used CDBG funds to cover the overhead of general technical assistance loans (non-CDBG-financed), we reviewed one of the 20 general technical assistance loans generated during program years 1999 to 2006. We also reviewed all four defaulted CDRLF loans. We examined all of the files provided by the Corporation for technical assistance and site search services. In addition, we evaluated whether the Corporation had adequate financial controls to safeguard CDBG funds, including the program income generated during our audit period. Further, we tested whether job creation national objectives were achieved for the economic development activities.

The audit generally covered the period June 1, 1999, through May 31, 2007. To accomplish our objectives, we extended the period back to the inception of the Corporation in the 1980s. We performed our audit fieldwork from December 2007 through April 2008 at the Corporation's office, located in the County's office building in Newark, New Jersey, located at the Hall of Records, 465 Dr. Martin Luther King, Jr., Boulevard, Newark, New Jersey.

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

# INTERNAL CONTROLS

---

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

---

## Relevant Internal Controls

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

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.
- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.



## Significant Weaknesses

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

- The Corporation did not have adequate controls over compliance with laws and regulations, as it did not always comply with HUD regulations while administering the economic development loan programs and disbursing CDBG funds (see finding 1).
- The Corporation did not safeguard resources, as it did not establish adequate financial controls to ensure adequate financial records, proper accounting for program income, and an adequate budget and cost allocation system (see finding 2).

## APPENDIXES

### Appendix A

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

<u>Recommendation number</u>	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>	<u>Funds to be put to better use 3/</u>
1A			\$662,184
1C	\$133,000		
1D		\$1,678,732	
Total	<u>\$133,000</u>	<u>\$1,678,732</u>	<u>\$662,184</u>

- 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 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. This includes reductions in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures, and any other savings which are specifically identified. In this instance, if the County implements our recommendation to establish and implement adequate procedures and controls over its economic development loan programs, it will be able to assure HUD and its citizens that the existing loan fund balances will be used in a timely manner to create jobs, facade improvements, and area benefits.

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

### Ref to OIG Evaluation

### Auditee Comments



**Economic Development Corporation  
of Essex County**

Hall of Records - Room 449  
465 Dr. Martin Luther King, Jr. Blvd.  
Newark, New Jersey 07102  
973-621-4454 • 621-2545 (Fax)

**BOARD OF TRUSTEES**

Alexander Quiceno, President  
Charles J. Stewart, Vice President  
Goldie Burbage, Secretary/Treasurer  
Jose Machado  
Floyd Melvin  
Lathia Morris  
Tendaj N'Doro, PhD  
Gerald Owens  
Marlene J. Waldock




**Deborah E. Collins, Esq.**  
Executive Director

**Craig Lombardi**  
Deputy Director

**Memorandum**

TO: Edgar Moore, Regional Inspector General for Audit

FROM: Deborah E. Collins, Esq., Executive Director 

DATE: October 14, 2008

RE: Draft Audit Report of the Economic Development Corporation's (EDC) Block Grant Program

On behalf of the Economic Development Corporation of Essex County and in response to your letter dated September 22, 2008 to Joseph N. DiVincenzo, Jr., County Executive, enclosed you will find the EDC's response to the draft audit report dated "September xx, 2008" submitted by Edgar Moore, Regional Inspector General for Audit, 2AGA.

Should you have any questions concerning this submission or require additional information, please contact Craig Lombardi at (973) 621-4454.

CC: Kathleen Naymola, Director, Community Planning and Development, 2FD  
Joseph Vizer, Assistant Regional Inspector General for Audit  
Joyce Wilson Harley, Esq., Essex County Administrator  
Craig Lombardi, Deputy Director  
Dominic J. Scaglione, Inspector General  
Michael Taylor, Director, Division of Housing and Community Development  
George Serio, Assistant Director, Division of Housing and Community Development

*"Putting Essex County First"*  
ESSEX COUNTY IS AN EQUAL OPPORTUNITY EMPLOYER

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

### Ref to OIG Evaluation

### Auditee Comments

#### EXECUTIVE SUMMARY: EDC RESPONSE TO HUD OIG AUDIT

The following is a summary of the response from the Economic Development Corporation of Essex County (EDC) to findings and concerns raised by the HUD Office Inspector General in a draft audit report prepared by Edgar Moore for Kathleen Naymola which reviewed EDC, a sub grantee of the Essex County Division of Housing and Community Development, for the program years from PY 1999 through PY 2006. Presented below are concerns highlighted in the draft audit report, responses from EDC regarding these concerns, and future objectives/actions proposed to address said concerns.

The following acronyms appear in this response:

CDBG	Community Development Block Grant
DHCD	Essex County Division of Housing and Community Development
EDC	Economic Development Corporation of Essex County
HUD	Department of Housing and Urban Development
OIG	Office of Inspector General
SBDAA	Small Business Development and Affirmative Action
LFC	Legal & Project Finance Committee – reviews/approves EDC loan projects
CDRLF	Community Development revolving Loan Fund
CERP	Community Economic Revitalization Program (for façade improvements)
GPR	Grantee performance report annually submitted to DHCD
WISOMMM	Women In Support of Million Man March – received CDRLF loan in PY 2005

#### EXECUTIVE SUMMARY

The EDC has historically worked closely with DHCD in order to ensure our activities are in compliance with HUD regulations. Moreover, the EDC is strongly committed to increasing productivity, enhancing budget and performance submissions, and continuing to help small businesses access credit in order to spur the creation of jobs for low to moderate income persons.

**CONCERN #1:** EDC did not properly administer economic development loan programs (CDRLF and CERP) and lacked productivity in making CDBG economic development loans

#### Comments:

- Since the inception of the CDRLF, EDC has closed 19 CDRLF loans totaling \$771K
- Total CDRLF funding of \$771K represents lump sum draw downs of \$453K plus recycled principal and interest payments; EDC has effectively loaned nearly twice the aggregate amount of lump sum draw downs
- Based on strong repayment histories, a current loan fund balance of \$342K is available for future CDRLF projects
- Total reported full time equivalent jobs created for low to moderate income persons for these projects is 59 (EXHIBIT A)
- Through May 2008, EDC closed 19 CERP loans totaling \$453K (post modification of CERP guidelines in 1990).

### Comment 1

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

**Comment 2**

- EDC closed a 20<sup>th</sup> CERP loan in September 2008 in the amount of \$25,000
- From PY 1999 through PY 2006, EDC closed 2 CDRLF, 1 CERP and 20 other non CDBG loans;
- From PY 1999 through PY 2006, EDC loan recipients (CDRLF and non CDRLF), reported the creation of 126 full time equivalent jobs that were filled by low to moderate income persons (EXHIBIT B)
- History indicates these CDBG loan programs have been utilized but with cycles of greater and lesser activity. EDC believes demand for these programs is increasing.
- EDC agrees that generating new loan activity for the CDRLF and CERP programs is a priority

**Future Objectives/Actions:**

Generate increased awareness and stimulate demand for CDBG loan programs by:

- Visiting with business owners at events hosted by business development organizations from municipalities eligible to receive CDBG funding
- Issuing press releases about closed loans such as the CERP loan just closed in West Orange
- Promoting programs via newspaper and local community cable station interviews
- Presenting programs to women and minority owned businesses presently working with SBDAA
- Addressing needs for commercial credit as conventional resources are forced to severely restrict their lending, thereby ensuring that area small businesses stay open and continue to add jobs for low to moderate income persons.

**Comment 3**

**CONCERN #2:** EDC received a duplicate drawdown (for CDRLF loan to JP Cleaners) and improperly converted a loan to a grant (for a CDRLF disbursement to WISOMMM).

**Comments re duplicate drawdown:**

- EDC acknowledges that in accordance with the historical processing of other CDRLF loans, and with the approval of DHCD, EDC executed a lump sum draw down for \$33,000 in order to reimburse the CDRLF account for loan proceeds disbursed to J&P Dry Cleaners. (EXHIBIT C)

**Future Action:**

- As per the recommendation of HUD, EDC will reallocate funds from the CDRLF account to the lump sum ledger maintained by DHCD in the amount of \$33,000.

**Comments re recoverable grant loan to WISOMMM:**

**Comment 4**

- The structure for this "recoverable grant loan" was based on similar projects funded by private corporations, agencies and foundations that were utilized specifically to address funding needs of not for profit organizations.

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

Comment 4

- The feasibility and credit worthiness of the WISOMMM proposal was reviewed and approved by the EDC LFC; WISOMMM had previously received funding of \$500,000 from Independence Community Bank
- Before disbursing funds from the CDRLF, EDC received the required approval from DHCD (EXHIBIT D).
- EDC acknowledges that CFR 570.203 (b) does not specifically reference a "recoverable grant loan" but it does allow for grants for special economic development activities. (EXHIBIT E)
- WISOMMM has submitted documentation indicating it has achieved the two required benchmarks of creating a minimum of 3 full time equivalent jobs and providing day care services to a minimum of students per month over a 12 month period. (EXHIBITS F, G, H)
- EDC acknowledges that at the time of the HUD audit, WISOMMM had not yet documented that it had achieved the job creation benchmark. However, based on affirmations from WISOMMM that it had created 3 jobs for low to moderate income persons and would be able to document the achievement of this loan performance benchmark, EDC did not declare the loan in default after the first year, nor did EDC officially convert the loan into a Recoverable Grant.

**Future actions:**

- Based on the information presented here and later in the body of this report, EDC requests that HUD reconsider its conclusion that the CDRLF funding should be reimbursed.

Comment 4

**CONCERN #3:**

EDC did not carry out adequate technical assistance (only 7 projects listed by auditors from PY 1999 through PY 2001) and site search services (no site search projects reported prior to PY 2004)

**Comment:**

Comment 5

- EDC delivered technical assistance to over 160 small businesses located in participating CDBG municipalities during the period extending from PY 1999 through PY 2006. (EXHIBIT I) and logged the time allocated for these projects
- The primary technical assistance services delivered by EDC are to consult businesses, assist in the preparation of business plan, and help secure loans in order to stimulate economic growth and create job opportunities for low to moderate income persons. Other technical assistance services (providing economic data to businesses, marketing Essex County as a desirable business location, educating and supporting small business in Essex County through conferences and meetings, site search assistance) have historically been categorized as general technical assistance activities. To date, more detailed data on these services has not been requested.

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

**Comment 5**

A breakdown of these technical assistance projects from PY 1999 through PY 2006 is as follows:

- 119 of the 161 projects reviewed by the auditors chose not to follow up with EDC after meeting with EDC and receiving a detailed business plan outline (**EXHIBIT J**)
- 35 clients interacted with EDC after their initial meeting in order to further discuss and develop their business expansion proposal. Although these projects did not result in the closing of an EDC loan, EDC delivered technical assistance that helped business owners set up their companies, prepare business plans, obtain alternative financing, and/or elect to cancel or postpone their projects. It is expected some may apply for a future loan. EDC believes these projects should be recognized as having received extensive technical assistance.
- 9 other projects should be recognized for receiving extensive technical assistance from EDC, but were not reviewed by the auditors because they did not see the case folders that were packed in a separate file box. Each of these clients received extensive assistance from EDC, with one of them (Supreme Bakery) eventually receiving a loan in September 2008.

**Comment 5**

EDC acknowledges that the 119 clients receiving nominal assistance from EDC cannot be categorized as special technical assistance projects, even though some may have independently completed business plans and made strategic decisions based on input from EDC. However, for clients that interacted with EDC for several sessions, their projects should be recognized for receiving technical assistance, in which case 44 projects would be designated with that description.

#### **Future Action/Objectives:**

- Generate more demand for technical assistance services by enhancing awareness of EDC programs and services
- Continue to document records of technical assistance projects utilizing the forms previously developed in consultation with HUD and DHCD, and add any additional data that HUD may recommend

**Comment 2**

#### **Comments re site search services**

- Prior to 2004, EDC experimented with various ineffective site search methods
- In 2004, EDC subscribed to a data base of available sites in Essex County. Since implementing this new program, the number of requests for site search assistance has increased.
- Historically, EDC has provided a general summary of site search projects in its annual GPR

**Comment 6**

#### **Future Plans/Objective**

- Stimulate greater demand for this service by enhancing customer awareness
- Provide more detailed information of site search clients in the EDC annual GPR

**Comment 6**



# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

**Comment 7**

**CONCERN #4**

EDC could not support that its activities met the CDBG national objectives

**Comments:**

- From PY 1999 through PY 2006, EDC loan recipients (CDRLF and non CDRLF), reported the creation of 126 full time equivalent jobs that were filled by low to moderate income persons
- In accumulating job creation data for CDRLF and other EDC loan recipients, EDC utilized documentation that was designed in conjunction with HUD and DHCD in response to recommendations from a prior HUD monitoring of EDC. **(EXHIBIT K)**
- EDC compilation of data was supported in a 1999 letter from HUD monitors which did not highlight any failures in EDC's compilation of job creation data utilizing said documentation and recognized the jobs created reported by CDRLF and non CDRLF loan recipients. **(EXHIBIT L)**
- Prior to the recent HUD OIG audit, EDC had not been advised that its job creation data collection process needed to be revised.
- Of the 126 full time equivalent jobs cited above, 19.5 were created by businesses that received EDC loans prior to PY 1999. For these projects completed during and after PY 1999, the ratio of total CDRLF and non-CDRLF loan dollars (\$1,282,411) to jobs created by those loan recipients is \$12,000 per job created, which beats the maximum performance standard of \$35,000 per job cited by HUD. Adding administrative costs covered by CDBG funds during this period (\$1,678,732) to total loans during this period (\$1,282,411) would yield a calculated dollar to job created ratio of would be \$27,804 per job created, which still exceeds the maximum performance standard of \$35,000 per job cited by HUD

**Future actions/objectives:**

Address concerns raised in audit regarding compilation of job creation data by:

- Acquire roster of employees at date of loan closing in order to compare roster to future employment records
- Define titles of job positions to be created in loan documentation (titles are included on current Employment Summary form)
- Confirm with business owners whether new person hired is filling a new position or replacing a former employee
- When applicable, utilize forms that have been approved for DHCD
- Check with employers on the status of persons previously reported as new hires

**Comment 2**

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

Comment 8

**CONCERN #5:**

EDC lacked evidence to justify its CDBG administrative expenses

**Comments:**

- From PY 1999 through PY 2006, EDC closed 3 CDBG funded loans and 20 other non CDBG loans, reported the creation of 126 full time equivalent jobs filled by low to moderate income persons (yielding a ratio of total loan and CDBG administrative funds to jobs created of \$27,000 per job), delivered technical assistance to over 160 clients, and enhanced its site search service.
- With the support of CDBG funds, EDC was able to deliver the loans cited above and support the creation of jobs for low to moderate income persons.
- All CDBG funds disbursed to EDC are backed up by vouchers and invoices submitted to DHCD; EDC has always provided full access to such documents.
- EDC will modify its presentation of budgets to show how costs are expended per activity
- EDC has historically prepared budgets in consultation with DHCD and delivered all documents requested and required by DHCD regarding annual expenditures. Furthermore EDC has worked to comply with any directives from DHCD.

**Future Actions/Objectives**

- Increase productivity
- Update presentation of budget to reflect HUD requirements; when applicable, utilize procedures and forms which DHCD and HUD have determined to be compliant with HUD regulations
- Submit supporting documentation for the CDBG activities carried out during program years 1999 to 2006 to affirm EDC is in compliance with HUD regulations and document the eligibility and reasonableness of the \$1,678,332 that EDC disbursed for administering its CDBG economic development activities during that period.

Comment 2

**CONCERN #6:**

EDC did not always comply with HUD requirements to ensure that (1) adequate financial records were maintained for its two economic development loan programs, (2) program income was properly accounted for; 3) adequate budget and cost allocation procedures were implemented. As a result, financial records were inadequately maintained; program income was improperly recorded; and CDBG funds were not properly budgeted, allocated, and safeguarded.

# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

---

### Ref to OIG Evaluation

### Auditee Comments

Comment 9

**Comments:**

- EDC has managed the CERP and CDRLF accounts in a satisfactory manner, and records are consistent with bank statements and ledgers from DHCD for the CDRLF and CERP accounts. (EXHIBITS M)

Comment 9

- EDC delivers bank statements and a summary of the account ledgers for CDRLF and CERP to DHCD. Furthermore, EDC has, and will continue to provide full access to DHCD to all financial records, and when necessary, reconcile any differences.

Comment 10

- EDC acknowledges there were a few clerical errors related to the depositing of CDRLF funds prior to 1995, but improved staff diligence and financial software have significantly diminished the potential for error.

Comment 9

- EDC presented applicable documents related to the start up and guidelines for CERP and CDRLF programs to the auditors. (EXHIBITS N & O)

Comment 4

- Draw downs from either the CERP or CDRLF programs are always subject to final authorizations by DHCD, and EDC will only draw down funds for projects approved by DHCD.

Comment 9

- Ledgers maintained by EDC are reconciled with bank statements on a monthly basis. Ledgers and/or bank statements have been periodically submitted to DHCD. To date, DHCD has not expressed any major concerns when EDC has submitted updated account statements, usually on a quarterly basis.

Comment 11

- EDC has provided DHCD the requested financial information about program income but the various sources of program income were reported separately via GPR reports, bank statements and ledger summaries rather than via a single presentation. Going forward, EDC will work with HUD and DHCD to develop a system designed to deliver this information in a concise, efficient manner.

Comment 9

- EDC will continue to send a summary of transactions and other information requested by DHCD to ensure the accounts are being managed correctly.

Comment 12

- In regards to the statement that EDC "incurred \$180,000 in CDBG expenses and more than \$1.5 million in non-CDBG expenses for program year 2005. ", it is noted that the non CDBG expenses of \$1.566 MM referenced here were comprised of \$1.414 MM in Individual Training Account Program Grants awarded to job training vendors, and do not include any operating expenses of EDC. The balance of approximately \$142K represented operating costs paid to EDC for processing these contracts. (EXHIBIT P)

**Future Activities/Objectives**

Comment 2

- Require Director of DHCD to provide signed approval of any loan disbursements from CDRLF / CERP accounts
- Establish consistent procedure for communicating information to DHCD and develop systems and procedures to ensure EDC is in compliance with HUD regulations and policies

## Appendix B

### AUDITEE COMMENTS AND OIG'S EVALUATION

---

#### Ref to OIG Evaluation

#### Auditee Comments

#### Comment 2

- Modify budget submissions of EDC in order to facilitate evaluation of performance against the funds provided for each activity. EDC will work with DHCD to document work done on various activities consistent with HUD guidelines.

## OIG Evaluation of Auditee Comments

- Comment 1** Corporation officials indicated that they had closed 19 CDRLF loans since the inception of the program (in the mid-1980s). They state that \$771,000 in funds represents a lump sum drawdown of \$453,000 and recycled principal and interest payments. They stated that the current loan fund balance of \$342,000 was available for future CDRLF projects. Corporation officials also state they generated 59 jobs for low to moderate income people from these projects. They also stated that they had closed 20 CERP loans and 20 non-CDBG loans and that the loan recipients had reported the creation of 126 full time equivalent jobs for low and moderate income people. Corporation officials believed the demand for these programs is increasing and that generating new loan activity for the CDRLF and CERP programs is a priority. However, the Corporation only closed a total of three CDRLF and CERP loans during our audit period for program years 1999 through 2006. Finding 2 explains the problems regarding adequate financial documentation for the two loan programs and that Corporation officials could not show that the information regarding the initial funding, financial transactions, and current balances for the two revolving loan programs was accurate. We did give credit for the non-CDBG loans in evaluating the Corporation's achievements (i.e., job creation objectives) for carrying out economic development activities. However, the Corporation officials' responsibility to originate a reasonable amount of CDBG loans cannot be replaced with the non-CDBG loans. In addition, regarding the claim for jobs created, the evidence provided did not always support that new jobs were created or whether old jobs were refilled. Thus, the evidence of job creation was not always sufficient.
- Comment 2** The actions of the Corporation officials are responsive to the finding.
- Comment 3** Corporation officials agreed to reimburse the \$33,000 duplicate drawdown for one CDRLF loan back to the Division of Housing and Community Development of Essex County.
- Comment 4** Regarding converting the CDRLF loan to a grant, Corporation officials stated that the feasibility and credit worthiness of the business proposal was reviewed and approved by the Corporation's Legal & Project Finance Committee, the business (WISOMMM) had previously received funding of \$500,000 from other sources or a private bank and the Division of Housing and Community Development of Essex County (DHCD) also approved the loan (Exhibit D). Corporation officials acknowledge that regulations don't reference a recoverable grant, but allows for grants for special economic development activities. As such, Corporation officials also acknowledged that at the time of the HUD OIG audit, the business that received the \$100,000 CDRLF loan in 2005 had not documented that it had achieved the job creation bench mark. However, at the exit conference the officials provided documentation that the business submitted evidence (Exhibit F) indicating that it had actually generated 3 full time and one part time job for low and moderate income people and had met the child care enrollment objectives

(Exhibits G and H). Therefore, Corporation officials did not immediately declare the loan in default after the first year, nor officially convert the loan into a grant. Accordingly, Corporation officials requested that HUD reconsider the conclusion that the CDRLF funding should be reimbursed based on information presented.

Regarding the credit worthiness of the business (WISOMMM) that received the loan, Corporation officials failed to mention in their comments that the business was fully leveraged with over \$4.5 million in funds borrowed from a bank; and that the bank refused to authorize the business to assume any additional debt including a loan from the Corporation, because the Corporation would hold liens subordinate to the bank against the property owned by the business. As such, the Corporation converted the loan into a “recoverable grant loan” without requesting any collateral. Further, verification of the documentation provided at the exit conference regarding the jobs created (Exhibit F) disclosed that the Corporation’s current job creation form cannot sufficiently support whether these jobs were newly created or whether they were just refilling existing positions or replacing former employees. Since the business did not provide sufficient evidence to show that it fulfilled the job creation requirement in accordance with the loan agreement the requirements for converting the loan to a grant were not satisfied. Accordingly, Corporation officials need to request additional supporting documents such as payroll data to verify whether these jobs were created and maintained for a reasonable time period. Further, given the highly leveraged financial condition of the business, the lack of collateral for the loan, and the fact that adequate documentation was not provided to support job creation, it is evident that EDC has exposed HUD CDBG funds to high risk, therefore, HUD should require the \$100,000 loan to be repaid.

**Comment 5** Corporate officials stated that EDC had provided technical assistance to over 160 small businesses for program year 1999 through 2006. Corporate officials also stated that services such as providing economic data to small business, marketing and educational activities have been categorized as general technical assistance and that detailed data on these services had not been requested. At the exit conference Corporation officials provided a listing of the businesses assisted (Exhibit I) and stated that they provided adequate technical assistance to 161 small businesses during the program years 1999 through 2006, even though 119 businesses did not choose to follow up with the Corporation after an initial meeting. Corporation officials also claimed that the time spent in meeting with the business owners should be credited, even if no loan was generated or business plan was completed. Corporate officials stated that nine other projects should be recognized as having received extensive technical assistance from EDC but had not been reviewed by the auditors because they had been packed in a separate file box. Corporation officials also stated that 44 projects interacted with EDC for several sessions and should be recognized for receiving technical assistance.

Review of the documentation provided by Corporation officials revealed that technical assistance was provided to 161 businesses for program years 1999

through 2006. The records provided by Corporation officials disclosed that over an eight year period a total of 481 hours was spent in assisting 154 businesses, which did not generate any measurable results such as business plans or loans. In comparison, the seven businesses that we considered received adequate attention or assistance obtained 665 staff hours of assistance from the Corporation. Therefore, we concluded that Corporation officials did not provide documentation to show that significant time was spent in assisting the 154 businesses that did not have a measurable output in terms of a loan or business plan and question the value of the assistance provided in terms of helping to increase economic development. Several requests were made for all the records pertaining to technical assistance but files related to general technical assistance were not provided. In addition, Corporation officials stated that we did not review nine files which were in a separate file box. However, at the exit conference Corporation officials agreed that these nine files were never delivered to HUD OIG auditors. It is the Corporation's responsibility to provide all the records requested by HUD OIG auditors, especially after numerous requests made by the auditors during the field work period. As such the files should be provided to HUD Field Office officials as part of the audit resolution process.

**Comment 6** Corporation officials explained that they tried various site search methods prior to 2004, but none of them were effective. However, after 2004 they subscribed to a data base of available sites in Essex County that increased the number of requests for site search services. Corporation officials agreed to stimulate greater demand for this service in the future and to provide more detailed information in the Corporation's annual GPR.

**Comment 7** Corporation officials stated that they reported 126 full time equivalent jobs and exceed the job creation requirements as stipulated in HUD regulations. In addition, the officials indicated that its compilation of job creation data was documented in conjunction with HUD and the Division of Housing and Community Development of Essex County, and they have not been advised that its job creation data collection process needed to be revised. As stated in the report, the current form used by Corporation officials to collect job creation data cannot demonstrate that the new person hired is filling a new position or replacing a former employee, therefore, the reported 126 jobs created might not be accurate. As a subgrantee of HUD CDBG program, the Corporation is responsible to ensure that the information reported to HUD is accurate. Thus, additional documentation is needed to show that the 126 jobs listed as created were not just the refilling of already existing positions, but were actual jobs created for a reasonable period of time, as required. Once these documents are received HUD can make an eligibility determination during the audit resolution process.

**Comment 8** In justifying its \$1.6 million CDBG administrative expenses incurred, Corporation officials stated that for program years 1999 through 2006, the Corporation closed 3 CDBG and 20 non-CDBG loans and created 126 full time equivalent jobs to low to moderated income people. Corporation officials stated all disbursements were properly supported by vouchers and invoices, which were



submitted to the Division of Housing and Community Development of Essex County. Corporation officials stated that they would modify its budget presentation to show how costs are expended per activity that they had complied with directions from the Division regarding budget and annual expenditures. However, since the Corporation only generated 3 CDBG-financed loans, provided technical assistance to 7 businesses, and carried out limited site search services for businesses during the audit period, we disagree that the Corporation's administrative costs were justified. In addition, Corporation officials' responsibility to generate a reasonable amount of CDBG loans cannot be replaced with the 20 non-CDBG loans it originated during the program years 1999 to 2006.

- Comment 9** Corporation officials stated that they have managed the CERP and CDRLF accounts in a satisfactory manner, records have been reconciled and are consistent with bank statements and ledgers, and the Division of Housing and Community Development of Essex County did not expressed any major concerns. Corporation officials stated that they would continue to send summary information to the Division of Housing and Community Development and other requested information to ensure the accounts are managed correctly. We disagree with Corporation officials because it did not adequately maintain records to support the initial funding or the establishment of the two revolving accounts. Also, the ledger provided by Corporation officials disclosed accounting errors and CDBG funds still remained in the non-CDBG account (see Comment 10). In addition, as stated in the audit report the County issued a noncompliance monitoring report in 2005, which indicated the weakness of the Corporation's financial system.
- Comment 10** Corporation officials acknowledged that there were some clerical errors in depositing CDRLF funds prior to 1995, but that improved staff diligence and software have diminished the potential errors. However, some loan payments were also not properly recorded and some loan repayments had been deposited into the non-CDBG financed revolving loan account. In the Corporation's later detailed response to the audit, Corporation officials identified that interest and late fees of \$1,379 still remained in its non-CDBG financed program and agreed to reimburse these funds to the CDBG-financed revolving loan fund account. The reimbursement of these funds should be addressed as part of the audit resolution process with HUD.
- Comment 11** Corporation officials stated that they had provided the Division of Housing and Community Development of Essex County the financial records about program income, through GPR reports and bank statements. However, Corporation officials did not determine the actual amount of the program income. Nevertheless Corporation officials agreed to work with HUD and the County to develop a system to deliver this information in a concise, efficient manner.
- Comment 12** Corporation officials indicated that in regards to the statement that "EDC incurred \$180,000 in CDBG expenses and more than \$1.5 million of non-CDBG expenses" that the Corporation had carried out a non-CDBG financed training

program with the total funding of \$1.566 million, of which the Corporation obtained approximately \$142,000 for operating costs. The Corporation's financial statements for program year 2005 indicated that the Corporation incurred more than \$180,000 of CDBG expenses and had over \$1.5 million of non-CDBG expenses. Our audit revealed that the Corporation did not have a proper cost allocation method to allocate salaries and overhead among programs. Corporation officials agreed to modify their budget submissions in order to facilitate evaluation of performance against the funds provided for each activity, and develop systems and procedures to ensure compliance with HUD guidelines which is responsive to the finding.