



Issue Date July 1, 2010
Audit Report Number 2010-NY-1012

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

FROM: *Edgar Moore*
Edgar Moore, Regional Inspector General for Audit, New York/New Jersey, 2AGA

SUBJECT: The City of Jersey City, NJ's Community Development Block Grant Funds Used for a Float Loan Did Not Comply With Applicable Regulations

HIGHLIGHTS

What We Audited and Why

We audited the City of Jersey City's (City) Community Development Block Grant (CDBG) float loan activity because during our capacity review of the City's CDBG funding under the American Recovery and Reinvestment Act of 2009, we noted that the City did not follow CDBG float loan regulations. Our audit objective was to determine whether the City ensured that CDBG funds used for the float loan complied with applicable rules and regulations.

What We Found

The City did not comply with applicable regulations and failed to take timely action when the float loan defaulted. Specifically, it did not (1) make a good faith effort to collect payment on the float loan in the amount of \$3.5 million, (2) identify a proper default remedy in case the float loan defaulted, (3) properly account for and report float loan program income to the U.S. Department of Housing and Urban Development (HUD), (4) follow the required steps when the terms of the float loan was extended, and (5) maintain adequate supporting documentation to show that the

national objective was met. This noncompliance occurred because the City misinterpreted the CDBG float loan regulations and believed that the float loan could be converted into a grant. As a result, \$3.5 million disbursed for the float loan was not repaid, and \$72,517 in program income generated from the float loan was not properly accounted for and reported to HUD.

What We Recommend

We recommend that the Director of HUD's New Jersey Office of Community Planning and Development instruct the City to reimburse the CDBG program from non-Federal funds in the amount of \$3.5 million for the defaulted float loan; provide supporting documentation related to \$72,517 in program income generated from the float loan to ensure that it is properly recorded, reported to HUD, and used for CDBG-eligible activities or repay this amount to the CDBG line of credit; establish adequate policies and procedures to ensure that the City complies with applicable CDBG float loan rules and ensures that the proper default remedy action is identified and exercised in a timely manner; develop written policies and procedures to ensure that timely payments on CDBG float loans (both principal and interest) and any resulting program income are appropriately recorded and used for eligible CDBG activities in compliance with HUD regulations; and provide the supporting documents to show that the CDBG national objective was met.

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 with HUD and City officials during the audit and at an exit conference held on June 3, 2010. City officials provided their written comments to our draft report on June 3, 2010. In their response, City officials generally disagreed with the findings.

The complete text of the City's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVE

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.

Regulations at 24 CFR (Code of Federal Regulations) 570.301(b) permit a grantee to use undisbursed funds in the line of credit within its CDBG program account, which are budgeted in statements or action plans for one or more activities that do not need the funds immediately, for unfunded activities. Such funds are referred to as the "float," and an activity that uses such funds is called a float-funded activity. The float-funded activity must meet all the same requirements that apply to CDBG activities and generally must be expected to produce program income in an amount at least equal to the amount of the floated funds used and must be repaid in 2.5 years.

The City of Jersey City (City) administers its community planning and development programs through the Division of Community Development. The City is a CDBG entitlement grantee that has received approximately \$8 million annually in the past 11 years. It is governed by a mayor and a nine-member council. The council serves a 4-year term contemporary to the mayor's.

We audited the City's CDBG float loan activity because during our capacity review of the City's CDBG funding received under the American Recovery and Reinvestment Act of 2009, we noted that the City did not follow CDBG float loan regulations. Our objective was to determine whether the City ensured that CDBG funds used for the float loan complied with applicable CDBG regulations.

RESULTS OF AUDIT

Finding 1: The City Did Not Comply With HUD Requirements Related to a CDBG Float Loan

The City did not comply with applicable regulations for a CDBG float loan. Specifically, it did not (1) make a good faith effort to collect payment on the float loan, (2) identify a proper default remedy in case the float loan defaulted, (3) properly account for and report float loan program income to the U.S. Department of Housing and Urban Development (HUD), (4) follow the required steps when the terms of the float loan was extended, and (5) maintain documentation to support that the national objective was met. This noncompliance occurred because the City misinterpreted the CDBG float loan regulations and believed that the float loan could be converted into a grant. As a result, \$3.5 million disbursed for the float loan was not repaid, and \$72,517 in program income generated from the float loan was not properly accounted for and reported to HUD.

A Good Faith Effort To Collect Payments on the Float Loan Was Not Made

Regulations at 24 CFR 570.301(b) permit a grantee to use undisbursed funds in the line of credit and its CDBG program account, which are budgeted in statements or action plans for one or more activities that do not need the funds immediately, for unfunded activities. Such funds are referred to as the “float,” and an activity that uses such funds is called a float-funded activity. The float-funded activity must meet all the same requirements that apply to CDBG activities and generally must be expected to produce program income in an amount at least equal to the amount of the floated funds used.

The City disbursed \$3.5 million for a float loan during November 2000. However, the loan agreement executed between the City and the subgrantee did not provide for repayment of the loan from program income within 2.5 years and did not include a repayment schedule. Regulations at 24 CFR 570.301(b)(2) and (3) specify that the float loans should be repaid from program income within 2.5 years. The subgrantee agreement indicated that the float loan was for a one year period but also stated the subgrantee could request an extension of the grant period. Also, the City did not ensure that the subgrantee was capable of generating program income in an amount at least equal to the amount of the float loan as required by regulations at 24 CFR 570.301(b). In addition, the full amount of program income projected to be generated from the float loan

activity was not listed as the source of program income contrary to regulations at 24 CFR 570.301(b)(3).

A Remedy in Case of Loan Default Was Not Identified

The City did not identify a default remedy in its action plan or an amendment to the action plan. The City was required to declare one of the four regulatory options it would take if the float-funded activity failed to generate the projected amount of program income on schedule as required at 24 CFR 570.301(b)(4). Instead, it had reprogrammed funding from other projects to finance the float loan. As a result, several projects were negatively impacted, and HUD and the City lost \$3.5 million because the funds were no longer available due to the default and lack of an appropriate default remedy. Therefore, we consider \$3.5 million as an ineligible cost because the City failed to comply with applicable rules and regulations, did not identify an appropriate default remedy, and did not take timely action when the float loan defaulted.

Program Income Was Not Properly Accounted For and Reported to HUD

The City did not adequately account for or report the receipts and expenditures of program income as required by regulations. Section 570.500(a)(1)(v) states that payments of principal and interest on loans made using CDBG funds are considered to be program income. The receipt and expenditure of program income are supposed to be recorded as part of the financial transactions of the grant program and may be retained by the recipient if the income is treated as additional CDBG funds subject to all applicable requirements governing the use of CDBG funds, as required by 24 CFR 570.504(a). Review of the City's consolidated plan annual performance report for program year 2002 showed that \$72,517 in program income was received from the float loan. However the City did not properly account for the program income and report it in HUD's Integrated Disbursement and Information System (IDIS); therefore, we could not determine how the program income was used. City officials did not recall how the program income was used, but stated that the funds would have been used for other eligible CDBG activities. As a result, there was no assurance that the City reported accurate CDBG program income and used this income in accordance with HUD regulations.

The Required Steps Were Not Followed When the Loan Terms Were Extended

The City extended the float loan for another year according to a resolution of the municipal council of the City, which authorized a 1-year extension up to September 2002. However, the City did not list and describe the new float-funded activity in its action plan or an amendment to the action plan as required. Regulations at 24 CFR 570.301(b)(2)(ii) state that any extension of the term for a float-funded activity shall be considered to be a new float-funded activity and may be implemented by the grantee only if the extension is made subject to the same limitations and requirements as applicable to a new float-funded activity. Section 570.301(b)(1) also states that each float-funded activity must be individually listed and described in the action plan. As a result, the City did not properly inform HUD and its citizens of changes to the float loan terms, which could impact the other community development activities that may depend on the funds from the float loan repayments. In addition, as with the original terms the City did not specifically require repayments or a default remedy in the extension as required.

Support for Meeting the National Objective Was Not Documented

The City did not maintain documentation to support that the national objective of low- and moderate-income job creation was met as provided by regulations at 24 CFR 570.208. City officials stated that the City did not have all of the files related to the float loan readily accessible. They later attempted to provide supporting documents, which showed that 176 positions—16 full time, and 156 part time, and 4 management positions—were created. However, it appeared that the documents provided pertained to a Section 108 loan job creation and also indicated that the jobs were created before the float loan funding was provided to the subgrantee. Thus, since the IDIS report for this activity showed that the City had proposed that 225 jobs would be created from the float loan project, the City failed to provide the equivalent number of full-time positions. Regulations at 24 CFR 570.209(b)(1)(i) require the grantee to create or retain at least one full-time equivalent permanent job per \$35,000 in CDBG funds used. Therefore, the City should have created the equivalent of 100 full-time jobs for the \$3.5 million used for the float loan-funded activity. Accordingly, there is no evidence that the float loan activity met the national objective of creation of low- and moderate-income jobs.

Conclusion

The City did not comply with applicable regulations for float-funded activities and failed to take timely action when the float loan defaulted. As a result, \$3.5 million disbursed for the float loan was not repaid, and \$72,517 in program income generated from the float loan was not properly accounted for and reported to HUD. This noncompliance occurred because the City misinterpreted the CDBG float loan regulations and believed that the float loan could be converted into a grant.

Recommendations

We recommend that the Director of HUD's New Jersey Office of Community Planning Division instruct the City to

- 1A. Establish adequate policies and procedures to ensure that proper default remedy actions, as required by regulations at 24 CFR 570.301(b)(4), are identified in its action plan and exercised in a timely manner when a float loan defaults.
- 1B. Reimburse the CDBG program from non-Federal funds in the amount of \$3.5 million representing the unrecovered principal of the defaulted float loan.
- 1C. Provide documentation related to \$72,517 in program income generated from the float loan to ensure that it is properly recorded and reported to HUD and used for CDBG-eligible activities or repay this amount to the CDBG line of credit.
- 1D. Develop written policies and procedures to ensure that timely payments on CDBG float loans (both principal and interest) and any resulting program income are appropriately recorded and used for eligible activities in compliance with HUD regulations.
- 1E. Provide the supporting documentation to show how the national objective of the CDBG program was met.
- 1F. Establish procedures to ensure that appropriate documentation is maintained to show that the national objectives of the CDBG program are met.

SCOPE AND METHODOLOGY

The objective of our review was to determine whether the City ensured that CDBG funds used for the float loan complied with applicable CDBG regulations.

To accomplish our objectives, we

- Reviewed applicable laws, regulations, and HUD program requirements at 24 CFR (*Code of Federal Regulations*) 570.
- Conducted interviews with City officials to gain an understanding of the internal controls related to the administration of its CDBG activities.
- Reviewed the City's program policies and procedures, action plans, HUD's monitoring report, independent accountant's audit reports, funding agreements, board of city council minutes, budgets, and general ledgers.
- Selected the float loan activity from the City's program year 2007 Consolidated Annual Performance and Evaluation Report (CAPER) and reviewed the related files to ensure compliance with program regulations and procedures

We performed our fieldwork from January to March 2010 at the City's office located at 30 Montgomery Street in Jersey City, New Jersey. Our audit generally covered the period from June 1, 2000 through September 30, 2003 and was expanded as necessary

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 an integral component of an organization's management that provides reasonable assurance that the following controls are achieved:

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. They 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 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 audit, we believe that the following item is a significant weakness:

The City had no policies and procedures on how to properly administer a float loan (See finding).

APPENDIXES

Appendix A

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

<u>Recommendation</u> <u>number</u>	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>
1B	\$3,500,000	
1C		\$72,517
Total	<u>\$3,500,000</u>	<u>\$72,517</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 the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

	<p>DEPARTMENT OF HOUSING, ECONOMIC DEVELOPMENT & COMMERCE DIVISION OF COMMUNITY DEVELOPMENT</p>
<p>JERRAMAH T. HEALY, MAYOR CITY OF JERSEY CITY</p>	<p>30 Montgomery Street, Suite 404, Jersey City, N.J. 07302 Phone: (201) 547-6910 Fax: (201) 547-5104</p>
<p>June 3, 2010</p>	
<p>Edgar Moore Regional Inspector General for Audit U.S. Department of Housing and Urban Development Office of Inspector General for Audit 26 Federal Plaza, Room 3430 New York, NY 10278-0068</p>	
<p>Re: The City of Jersey City – CDBG Float Loan Martin Luther King Drive Retail Plaza</p>	
<p>Dear Mr. Moore:</p>	
<p>The City has reviewed the Office of the Inspector General's draft audit report. Your report focused on a float loan awarded to the Martin Luther King Drive Joint Venture Partnership (MLK/JVP) for the Martin Luther King Drive Retail Plaza. You stated that the City did not comply with applicable regulations and failed to take timely action when the float loan defaulted. The following is background information on the MLK Drive Retail Plaza and the City's responses to your comments and recommendations.</p>	
<p>The MLK Drive Retail Plaza (the "Plaza") is an 85,000 sq. ft. shopping center that was completed approximately ten (10) years ago. The development area is six (6) blocks long comprised of eighteen (18) acres. The Plaza was one of the most anticipated projects to be developed in the most depressed section of the City. The service area is primarily low / moderate income (52%) and contains primarily minority households. Development of the Plaza was a major effort to bring hope to the Martin Luther King Drive area. CDBG float loan funding was essential to complete construction and keep the Plaza operational. Without the \$3.5 million infusion of float loan financing, the project would have failed. This would have had a devastating impact on an area of the City that has experienced tremendous disinvestment during the past 35+ years. In addition, millions of dollars in federal and state financing would have been lost as a result of a failed project.</p>	
<p>The purpose of the float loan was to complete the construction of the shopping center tenant fit outs. In addition, the float loan covered financing costs, maintenance, security, taxes and related soft costs. All work was to be completed by December 2000. The loan had a one (1) year term with the option to extend it up to one (1) additional year.</p>	
 <p>IT'S IN OUR HANDS</p>	

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Re: MLK Drive Retail Plaza
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The loan qualified as a special economic development activity as described in 24 CFR 570.203(a). The National Objective was low / moderate income area as described in 24 CFR 570.208(a)(1)(i). The City was careful to insure that the activity met the required public benefit test. According to this requirement, the amount of CDBG funds provided for the activity cannot exceed \$1,000 per low / moderate income person served. The City invested \$3.5 million in float loan financing. However, the City could have invested a maximum of \$5,925,500 (Number of L/M persons 16,930 x \$350 = \$5,925,500).

Monies earmarked for the CDBG float loan were reallocated from City sponsored activities, autonomous agency projects and cancelled projects. The float loan did not adversely impact on any CDBG eligible activities.

The following are the City's responses to specific comments in your audit:

OIG COMMENT

The City did not make a good faith effort to collect payment on the float loan in the amount of \$3.5 million.

CITY'S RESPONSE

The City exercised due diligence in an attempt to collect on the float loan. The float loan was issued in 2000 and it was extended for one (1) year until September 2002. Shortly thereafter, the Plaza experienced numerous setbacks. The anchor tenant ceased operating and several businesses closed. This made it very difficult for the (MLK/JVP) to service debt on the project.

Originally, MLK/JVP planned to sell equity in the Plaza to a private investor. The equity investment did not come to fruition. In spite of this, the City continued to correspond with the MLK/JVP about unresolved issues including the past due Float Loan. In August 2004, the matter was referred to the City's Law Department to initiate legal action. After numerous attempts to resolve matters with the MLK/JVP, the City issued a notice of default on June 24, 2005. Effective January 2007, the City, through the Jersey City Redevelopment Agency (JCRA), assumed control of the Plaza. JCRA engaged Brandywine Real Estate Corporation (BREC) to manage the Plaza. While BREC has been diligent in addressing outstanding issues related to the Plaza, the project has not generated sufficient revenue to repay the float loan.

OIG COMMENT

A remedy in the event of Loan Default was not identified.

CITY'S RESPONSE

The City acknowledges that we failed to identify a default remedy in the Action Plan or amendment to the Action Plan. The City further recognizes that there were no options for remedies except 24 CFR 570.301(b)(4)(i). This remedy allows for the amendment or deletion of activities in an amount equal to any default or failure to produce sufficient income in a timely manner. All other remedies would not have been financially feasible as the project was in a very tenuous state.

Comment 1

Comment 2

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AUDITEE COMMENTS AND OIG'S EVALUATION

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Auditee Comments

Comment 2

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The City did reprogram funds from other projects to finance the Float Loan, however, no projects were negatively impacted. In fact, approximately 65% of funding for the Loan came from a City autonomous agency – Jersey City Redevelopment Agency (JCRA) projects (59%) and City administration (6%). Eleven percent (11%) of funds came from MLK/JVP activities and 14% and 10% came from projects that were completed at a later date and cancelled activities, respectively. The City carefully chose projects that were more flexible to prevent an adverse impact on the City.

OIG COMMENT

Program Income was not properly accounted for and reported to HUD.

CITY'S RESPONSE

As stated in your correspondence, the program year 2002 CAPER showed that \$72,517 in program income was received. As required, the City reports all program income in IDIS. Based on our understanding of how IDIS operated at the time, monies generated as a result of program income were automatically added to the City's line of credit. When the City processed draw downs, program income was automatically applied to CDBG eligible activities. The current system allows you to specify which activity program income is applied to. This was clearly not the case back in 2002. As a result, we are unable to pinpoint a specific activity that the float loan income was applied against. The City accurately reported income as it came in and the income was applied to CDBG eligible activities.

Comment 3

OIG COMMENT

The required steps were not followed when the loan terms were extended.

CITY'S RESPONSE

The City did advertise the amendment as required by HUD. However, the City acknowledges that the extension of the term of the float loan was not treated as a new activity as set forth in 24 CFR 570.301(b)(2)(ii). The City made several efforts to help stabilize the MLK Drive Retail Plaza. Actions taken by the City included, but were not limited to, taking possession of the MLK Drive Retail Plaza as a remedy of default, appointing JCRA as the receiver to operate the Plaza – JCRA engaged Brandywine Real Estate Corporation (BREC) to manage the Plaza. In 2005, City offices were relocated to vacant space in the Plaza to increase foot traffic. The City has paid in excess of \$125,000 annually in City dollars to stabilize the project. Also, non-compliant tenants were evicted. These actions were taken to improve the viability of the Plaza.

Comment 4

OIG COMMENT

Support for meeting the National Objective was not documented.

CITY'S RESPONSE

The service area for the MLK Drive Retail Plaza is a primarily low / moderate income area. The City erroneously set up the activity in IDIS as an activity that qualifies based on low / moderate income jobs. However, as noted in the attached City Council resolution project description sheet, the activity qualified based on low / moderate income area (See Attachment 1). The City further verified this by communicating with the HUD Representative - [REDACTED] (See Attachment 2). As required, the City documented the file to verify that the activity qualified based on low / moderate income area according to 24 CFR 570.208(a)(1)(i) (See Attachment 3).

Comment 5

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AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 6

Re: MLK Drive Retail Plaza
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The following addresses specific recommendations:

- 1A. Establish adequate policies and procedures to ensure that proper default remedy actions, as required by regulations at 24 CFR 570.301(b)(4), are identified in its action plan and exercised in a timely manner when a float loan defaults.**

Be advised that the City does not intend on funding any float loans at this time. If the City chooses to do so in the future, we will consult with HUD for guidance.

- 1B. Reimburse the CDBG program from non-Federal funds in the amount of \$3.5 million representing the unrecovered principal of the defaulted float loan.**

While the City has been unable to recover the \$3.5 million awarded to the MLK/JVP, the funds were invested in a very important project that is serving a primarily low/moderate income population.

As previously noted, the float loan was used to cover construction related costs for the MLK Drive Retail Plaza. The loan made it possible for the developer to complete the project, which opened in February 2001. If the City had not provided float loan financing for this eligible activity, the project would have failed. The City acknowledges that technical errors were made in executing this activity. However, the City did perform its due diligence to insure that this activity met a National Objective and passed the public benefits test required for Special Economic Development Projects.

HUD has multiple remedies at its disposal for addressing deficiencies identified during this review. The City strongly disagrees with your recommendation to reimburse the CDBG program from non-federal funds in the amount of \$3.5 million. The City is prepared to amend Action Plans and take any other action HUD deems appropriate to remedy this situation. However, reimbursement of funds spent on an eligible activity in the most depressed section of the City is an unreasonable and excessive requirement.

Again, the float loan was used to complete the MLK Drive Retail Plaza. The funds were spent on eligible activities which allowed this development to open for business and remain open. When the developer was declared in default of its obligation, the City took the appropriate action to take possession of this asset. As a result of the City's actions, we have been able to preserve this project which is heavily subsidized by Federal resources.

- 1C. Provide documentation related to \$72,517 in program income generated from the float loan to ensure that it is properly recorded and reported to HUD and used for CDBG-eligible activities or repay this amount to the CDBG line of credit.**

The City reported program income in IDIS as required. In 2002, IDIS did not allow communities to specify which activity program income was applied to. Program income was automatically applied to eligible activities as draw downs were processed. The City

Comment 3

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Auditee Comments

Comment 6

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is prepared to work with the appropriate HUD staff to ascertain if it is possible to track program income expenditures that occurred in 2002.

- 1D. Develop written policies and procedures to ensure that timely payments on CDBG float loans (both principal and interest) and any resulting program income are appropriately recorded and used for eligible activities in compliance with HUD regulations.**

The City does not intend on funding any more float loans, at this time. If the City chooses to do so in the future, we will consult with HUD.

Comment 5

- 1E. Provide the supporting documentation to show how the national objective of the CDBG program was met.**

As previously stated, the project qualifies as low / moderate income area. See Attachment 3 for documentation verifying compliance with the National Objective.

Comment 6

- 1F. Establish procedures to ensure that appropriate documentation is maintained to show that the national objectives of the CDBG program are met.**

The City does not intend on funding any more float loans, at this time. If the City chooses to do so in the future, we will consult with HUD.

Sincerely,



Darice Toon
Director

cc: John Kelly, Business Administrator – City of Jersey City
Rosemary McFadden, Deputy Mayor – City of Jersey City
Carl Czaplicki, Director – HEDC

Attachments

DT:sah

OIG Evaluation of Auditee Comments

- Comment 1** Although City officials stated that they took action to collect the float loan, including declaring a default and initiating legal action, they did not provide any supporting documents during the audit and at the exit conference to show that good faith efforts were made to collect the float loan payment. Regulations at 24 CFR 570.301(b)(2) and (3) specify that float loans should be repaid from program income within 2.5 years, and the grantee must include in its action plan the full amount of expected program income from these activities. The City did not repay the float loan within 2.5 years and also the loan agreement executed between the City and the subgrantee did not provide for repayment of the loan from program income within 2.5 years. As such, the \$3.5 million is an ineligible cost which needs to be repaid to the CDBG program regardless of what efforts were made to collect the float loan.
- Comment 2** The City officials acknowledged that they did not identify one of the four regulatory default options in the action plan or amendment to the action plan. They stated that only one of the default options which allows for the amendment or deletion of activities in an amount equal to any default or failure to produce sufficient income in a timely manner was feasible. However, the City did not exercise this option in a timely manner. Further, Regulations at 24 CFR 570.301(b)(4)(i) require that if the grantee makes this choice, it must include a description of the process it will use to select the activities to be amended or deleted and how it will involve citizens in that process; and it must amend the applicable statement(s) or action plan(s) showing those amendments or deletions promptly upon determining that the float funded activity will not generate sufficient or timely program income. City officials indicated that funds were reprogrammed from other activities to finance the float loan and that no projects were negatively impacted. However, funds used for the float loan, which were not repaid, were not available for other eligible community development activities and other activities had to be delayed because the funds were not available.
- Comment 3** Review of the City's program income report obtained from the HUD's Integrated Disbursement and Information System (IDIS) did not show that \$72,517 of the program income was recorded and properly accounted for. As such, since the program income was not recorded in IDIS, HUD has no assurance that it was used for eligible CDBG activities; accordingly our recommendation stands.
- Comment 4** City officials acknowledged that the extension of the term of the float loan was not treated as a new activity as required by regulations at 24 CFR

570.301(b)(2)(ii). They also did not specifically require repayment of the float loan or specify a proper default remedy option. City officials indicated a number of actions that were taken, which improved the viability of the float loan funded activity; however, the actions taken were not an effective default remedy as the float loan was not repaid.

- Comment 5** City officials stated that national objective was erroneously set up as an activity that qualifies based on low/moderate income jobs when it should have been set up as qualifying based on a low/ moderate income area benefit as communicated to a former HUD official. In addition, although the City resolution, which extended the float loan, made reference to the area wide benefit, it also indicated that the float loan was required to create 225 full time jobs. Nevertheless, City officials were not able to provide any documents to show that HUD approved the change in the national objective and also did not change the national objective in the HUD's Integrated Disbursement and Information System (IDIS). Therefore, there was no evidence that the float fund activity was changed for the area wide benefit or that it met the national objective of creation of low/moderate income jobs. Furthermore, even if the float funded activity had been approved for the area wide benefit, since the loan had not been repaid in 2.5 years as required, the use of the funds was ineligible. Thus the funds should be repaid to the CDBG line of credit.
- Comment 6** The City does not plan to fund any more float funded activities and will consult with HUD if the City chooses to engage in float funded activities. This action is responsive to the finding, however, if the City decides to have float funded activities in the future it should submit the new procedures for approval by HUD prior to engaging in float funded financing.
- Comment 7** City officials acknowledged that errors were made in executing the float funded activity; however, they strongly disagree with reimbursing the funds spent. Nevertheless, City officials did not provide any documentation to support that good faith efforts were made to collect payment on the loan, the float fund activity met the national objective of low moderate income job creation, or evidence of HUD approval to change the activity to a low/moderate area benefit. Regulations at 24 CFR 570.301(b)(2) and (3) specify that float loans should be repaid from program income within 2.5 years, therefore, since the City did not identify any default remedy and failed to recover the loan funds as required, we consider \$3.5 million as an ineligible cost.