Issue Date August 5, 2010
Audit Report Number 2010-CH-1011

TO: Ray E. Willis, Director of Community Planning and Development, 5AD

//signed//

FROM: Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: The State of Illinois Needs To Improve Its Capacity To Effectively and Efficiently Administer Its Neighborhood Stabilization Program

HIGHLIGHTS

What We Audited and Why

We audited the State of Illinois' (State) Neighborhood Stabilization Program (Program). The audit was part of the activities in our fiscal year 2010 annual audit plan. We selected the State based upon citizens' complaints to our office. Our objectives were to determine whether the State (1) had the capacity to effectively and efficiently administer its Program and obligate Program funds before the required 18-month obligation deadline, (2) awarded Program funds for eligible projects, and (3) used Program funds for eligible administrative costs.

What We Found

The State needs to improve its capacity to effectively and efficiently administer its Program. Although the Illinois Housing Development Authority (Authority), the current administrator of the State's Program, had sufficient staffing levels and extensive experience with U.S. Department of Housing and Urban Development (HUD) programs, it is at risk of not meeting the required 18-month obligation deadline for Program funds. Further, the Illinois Department of Human Services (Department), the former administrator of the State's Program, allocated more than $4.8 million in Program funds for a project that did not comply with HUD's and Federal requirements for maintaining sufficient documentation to support the use of nearly $8,000 in Program funds for administrative expenses.

As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State, and HUD lacked assurance that the State used nearly $8,000 in Program funds for eligible Program administrative costs.

We informed the Authority's executive director and the Director of HUD's Chicago Office of Community Planning and Development of a minor deficiency through a memorandum, dated August 4, 2010.

What We Recommend

We recommend that the Director of HUD's Chicago Office of Community Planning and Development require the State to (1) implement adequate procedures and controls to ensure that it obligates its Program funds for eligible projects before September 4, 2010; (2) implement the Authority's Program reallocation award plan (plan) for the more than $4.8 million in Program funds available after the Authority rescinded one of the Department's allocations for a project; (3) provide sufficient supporting documentation or reimburse its Program from non-Federal funds, as appropriate, for the nearly $8,000 in Program funds used for unsupported administrative costs; and (4) implement adequate procedures and controls to address the finding cited in this report.

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 our discussion draft audit report and/or a supporting schedule to the executive director of the Authority, the chairman of the members of the Authority, and HUD's staff during the audit. We held an exit conference with the Authority's executive director on July 6, 2010.

We asked the Authority's executive director to provide comments on our discussion draft audit report by July 16, 2010. The executive director provided written comments, dated July 16, 2010. The executive director only partially agreed with the finding. The complete text of the written comments, except for 78 pages, including comments provided by the Department's general counsel, that were not necessary to understand the executive director's comments, along with our evaluation of that response, can be found in appendix B of this report. We provided the Director of HUD's Chicago Office of Community Planning and

Development with a complete copy of the Authority's written comments plus the 78 pages of documentation.

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BACKGROUND AND OBJECTIVES

The Program. Authorized under section 2301 of Title III of the Housing and Economic Recovery Act of 2008 (Act), as amended, Congress appropriated $4 billion for the Neighborhood Stabilization Program (Program) to provide grants to every State and certain local communities to purchase foreclosed-upon or abandoned homes and to rehabilitate, resell, or redevelop these homes to stabilize neighborhoods and stem the decline in value of neighboring homes. The Act states that amounts appropriated, revenues generated, or amounts otherwise made available to States and units of general local government under section 2301 shall be treated as though such funds were Community Development Block Grant (Block Grant) funds under Title I of the Housing and Community Development Act of 1974. The U.S. Department of Housing and Urban Development (HUD) allocated more than $3.9 billion in Program funds to more than 300 grantees.

Congress amended the Program and increased its funding as part of the American Recovery and Reinvestment Act of 2009 (Recovery Act). The Recovery Act provided HUD an additional $2 billion in Program funds to competitively award to States, local governments, nonprofit organizations, or consortia of nonprofit organizations, which could submit proposals in partnership with for-profit organizations. The Recovery Act also states that HUD's Secretary may use up to 10 percent of the funds for capacity building of and support for local communities receiving Program funding under the Act or the Recovery Act. Further, up to 1 percent of the funds shall be available to HUD for staffing, training, providing technical assistance, technology, monitoring, travel, enforcement, research, and evaluation activities. In January 2010, HUD awarded 56 organizations more than $1.9 billion in funds through a competitive process.

The State. The State of Illinois' (State) former governor initially designated the Illinois Department of Human Services (Department) as the administrator of the State's Program. The Department was created by the Illinois General Assembly in 1997 under the laws of the State. It is directed by a secretary appointed to a 2-year term by the governor and confirmed by the State Senate. The Department's overall mission is to assist customers in achieving maximum self-sufficiency, independence, and health through the provision of seamless integrated services for individuals, families, and communities. The Department's records are located at 401 South Clinton Street, and 100 West Randolph, Chicago, IL, and 100 South Grand Avenue East, Springfield, IL.

On November 12, 2009, the current governor reassigned administration of the State's Program to the Illinois Housing Development Authority (Authority). The Authority was created by the Illinois General Assembly in 1967 under the laws of the State. It is governed by a six-member board appointed to staggered 4-year terms by the governor and confirmed by the State Senate. The Authority's overall mission is to increase the supply of quality affordable housing for people of low and moderate means in the State. The Authority's records are located at 401 North Michigan Avenue, Chicago, IL.

HUD allocated more than $53.1 million in Program funds to the State based upon the funding formula developed by HUD pursuant to the Act. On March 4, 2009, HUD entered into a grant agreement with the Department for the full amount allocated. On September 2, 2009, the Department allocated nearly $47.3 million in Program funds to 18 entities for Program projects. HUD entered into an amended Program grant agreement with the Authority on December 8, 2009. The Authority entered into grant agreements with 17 of the 18 entities from April 6 through May 20, 2010. The grant agreements totaled nearly $42.5 million in Program funds. The Authority set aside nearly $517,000 in Program funds as a contingency reserve for the projects. On May 14, 2010, the Authority rescinded the Department's allocation of more than $4.8 million in Program funds to 55th and State Redevelopment, LLC (Redevelopment).

Further, as part of a consortium, the State submitted an application to HUD, dated July 15, 2009, which totaled nearly $35.3 million in additional Program funds under the Recovery Act. On January 14, 2010, HUD awarded more than $18.5 million in Program funds to the consortium. The Rock Island Economic Growth Corporation (Corporation) will serve as the lead agency to administer the Program. The Authority will primarily assist the Corporation with oversight, monitoring, and compliance with Federal requirements.

The citizens' complaints to our office alleged that the State's use of Program funds for administrative costs was questionable and its award of Program funds was inappropriate.

Our objectives were to determine whether the State (1) had the capacity to effectively and efficiently administer its Program and obligate Program funds before the required 18-month obligation deadline, (2) awarded Program funds for eligible projects, and (3) used Program funds for eligible administrative costs.

RESULTS OF AUDIT

Finding: The State Needs to Improve Its Capacity To Effectively and Efficiently Administer Its Program

Although the Authority had sufficient staffing levels and extensive experience with HUD programs, it is at risk of not meeting the required 18-month obligation deadline for Program funds. Further, the Department allocated more than $4.8 million in Program funds for a project that did not comply with HUD's requirements and did not comply with Federal requirements for maintaining sufficient documentation to support the use of nearly $8,000 in Program funds for administrative expenses. These weaknesses occurred because the Department and/or the Authority lacked adequate procedures and controls to ensure that Program funds would be obligated before the 18-month obligation deadline and Federal requirements were properly followed. As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State, and HUD lacked assurance that the State used nearly $8,000 in Program funds for eligible Program administrative costs.

The Authority Must Obligate Nearly $20.9 Million in Program Funds by September 4, 2010

Although the Authority had sufficient staffing levels and extensive experience with HUD programs, it is at risk of not meeting the required 18-month obligation deadline for Program funds. According to the Federal Register, dated October 6, 2008, each grantee must obligate its Program funds within 18 months of HUD's signing the Program grant agreement with the grantee. In addition, HUD's Program policy alert, volume 3, dated April 2010, states that HUD generally does not consider Program funds to be obligated for a specific activity unless the obligation can be linked to a specific address and/or household. Program funds are not obligated for an activity when subawards or grants to subrecipients or units of general local government are made.

As previously stated, on March 4, 2009, HUD entered into a grant agreement with the State's Department for more than $53.1 million in Program funds. On September 2, 2009, the Department allocated nearly $47.3 million in Program funds to 18 entities for Program projects. The Authority entered into grant agreements with 17 of the 18 entities from April 6 through May 20, 2010. It set aside nearly $517,000 in Program funds as a contingency reserve for the projects. Further, none of the grant agreements identified specific properties for the Program projects and only 8 of the 17 entities' proposals identified specific properties for the Program projects. On May 14, 2010, the Authority rescinded the Department's allocation of more than $4.8 million in Program funds to Redevelopment. The Authority developed a Program reallocation award plan (plan) for the more than $4.8 million in Program funds.

As of July 23, 2010, the Authority had obligated more than $26.9 million of the State's more than $47.8 million in Program funds set aside for Program projects.

The Department Allocated More Than $4.8 Million in Program Funds for an Ineligible Project

On September 2, 2009, the Department issued an award letter to Redevelopment allocating $4,833,000 in Program funds for the redevelopment of the Schulze Baking Company building, a commercial building located at 40 East Garfield Boulevard, Chicago, IL. Redevelopment planned to convert the Schulze Baking Company building into a mixed use building with commercial space and rental housing for low- and moderate-income households. However, the project did not comply with HUD's requirements.

The Federal Register, dated October 6, 2008, states that eligible uses for Program funds include the following: (1) the establishment of financing mechanisms for the purchase and redevelopment of foreclosed-upon homes and residential properties, including such mechanisms as soft-seconds, loan-loss reserves, and shared-equity loans for low- and moderate-income home buyers; (2) the purchase and rehabilitation of homes and residential properties that have been abandoned or foreclosed upon to sell, rent, or redevelop such homes and properties; (3) the establishment of land banks for homes that have been foreclosed upon; (4) the demolition of blighted structures; and (5) the redevelopment of demolished or vacant properties.

On December 14, 2006, Maktub Chicago Development, LLC (Maktub), purchased from the Chicago Baking Company a commercial property that included the Schulze Baking Company building; a detached retail building located at 10 East Garfield Boulevard, Chicago, IL; and a lot behind the detached retail building. On December 28, 2006, Maktub transferred the entire commercial property to Redevelopment under a single deed. Further, there were 15 parcel identification numbers associated with the commercial property. The Schulze Baking Company building was located on all 15 of the parcels. Therefore, Redevelopment's project would only qualify as an eligible Program project if the entire commercial property was vacant. However, the commercial property was not vacant.

On February 9, 2010, the Authority rescinded the Department's allocation of more than $4.8 million in Program funds to Redevelopment based on concerns with the financial feasibility of the project and Redevelopment's capacity to obligate Program funds within the required 18-month obligation deadline. HUD's Chicago Office of Community Planning and Development asked the Authority to reconsider Redevelopment's proposal due to concerns expressed by community leaders and the need for revitalization in the neighborhood. Therefore, the Authority did not follow through with its February 9, 2010, rescission of the Department's allocation to Redevelopment and continued working with Redevelopment to ensure that Redevelopment would be able to meet HUD's obligation and disbursement requirements for Program funds.

On April 14, 2010, we conducted a site visit to the commercial property. The first floor of the Schulze Baking Company building contained a remote control car race track with racing banners, an enclosed area with tables and chairs, and a skateboard area with ramps and a rail. The building's garage contained five vehicles. Further, the detached retail building contained office space, and construction vehicles were on the lot behind the detached retail building.

Redevelopment's managing member said that he and his friends raced remote control cars as a hobby and hung the banners to make the space feel like a real race track. They used the enclosed area to build and repair remote control cars. The skateboard area was also for him and his friends. He used the office space in the detached retail building to operate his three businesses: Maktub; Spirit Wrecking and Excavating, Inc.; and New South Partners, LLC. The construction vehicles on the lot behind the detached retail building were from Spirit Wrecking and Excavating, Inc. On May 7, 2010, the managing member provided a picture showing that an additional vehicle was in the Schulze Baking Company building's garage. He also provided documentation to support that three of the vehicles were owned by a partnership that included him and another partner for the purpose of conducting the general business of acquiring antique automobiles as a hobby. Two of the remaining vehicles were owned by either the other partner or an individual related to the other partner. The managing member could not provide ownership information for the sixth vehicle.

The Authority's senior policy director stated that since the Authority was not designated as the administrator of the State's Program until November 2009, the Authority decided to review all of the proposals for which the Department had allocated Program funds to ensure that the projects were eligible and would meet HUD's obligation and disbursement requirements.

As of May 7, 2010, the Authority was still working with Redevelopment to ensure that Redevelopment would be able to meet HUD's obligation and disbursement requirements for Program funds. The Authority did not have a concern with the eligibility of the project regarding the vacancy of the property. On May 14, 2010, and as a result of our audit, the Authority rescinded the Department's allocation of more than $4.8 million in Program funds to Redevelopment. On May 27, 2010, the Authority provided its plan for the more than $4.8 million in Program funds. The plan stated that the funds would be available to the State's Program recipients and Program recipients in the State that were funded directly by HUD under the Act. To be eligible for additional Program funds, the entities must demonstrate progress in the implementation of their current Program scope of work and/or projects and a clear capacity to implement additional eligible Program projects in areas of greatest need within the obligation, production, and expenditure deadlines for the Program. The State would also consider allowing the Authority to directly implement eligible projects with the reallocated funds. The plan also stated that the Authority would request information for the additional eligible Program projects beginning May 24, 2010, and continue accepting information through August 30, 2010. The Authority would award the reallocated Program funds on a rolling basis, subject to the availability of funding, based on the qualifications of the entities and the documentation provided. The senior policy director said that the Authority informed the State's Program recipients of the reallocated Program funds during update meetings and was working with HUD's Chicago Office of Community Planning and Development to identify possible projects associated with the Program recipients in the State that were funded directly by HUD.

The Department Lacked Documentation To Support Nearly $8,000 in Administrative Expenses

We reviewed all of the State's administrative expenses for the period March 2009 through March 2010, which totaled $539,544 in Program funds. HUD's regulations at 24 CFR (Code of Federal Regulations) 570.506(h) require grantees to maintain evidence to support how Block Grant funds are expended, and Office of Management and Budget Circular A-87 requires all costs to be necessary, reasonable, and adequately documented. The Department lacked sufficient documentation to support that it used $7,938 in Program funds from July through August 2009 for eligible Program administrative costs. The unsupported disbursements included wages for technical assistance personnel ($2,313) and the Department's Program accountant ($5,625).

The State Lacked Adequate Procedures and Controls

The weaknesses regarding the obligation of Program funds, allocation of Program funds for an ineligible project, and lacking documentation to support that administrative costs were eligible occurred because the Department and/or the Authority lacked adequate procedures and controls to ensure that Program funds would be obligated before the 18-month obligation deadline and were allocated

for an eligible project, sufficient documentation was maintained to support administrative costs, and Federal requirements were properly followed.
The Authority's senior policy director stated that the Authority had not obligated Program funds for projects due to its not having been designated as the administrator of the State's Program nearly 9 months into the 18-month obligation period. The Department allocated the Program funds to 18 entities before the Authority started administering the Program. Therefore, while preparing to administer its Program, the Authority focused on performing its due diligence by reviewing the entities' proposals and working with the entities to ensure that the projects were eligible and would meet HUD's obligation and disbursement requirements.

The senior policy director said that the Authority did not question the eligibility of Redevelopment's project regarding the vacancy of the property since the Program funds were only going to be used to redevelop the Schulze Baking Company building. Although Redevelopment's personnel were using the Schulze Baking Company building for recreational purposes, the Authority considered the building vacant since there were no legal occupants of the building.

The Department's chief financial officer said that the Department used nearly $6,000 in Program funds for wages for a temporary employee who provided accounting services. Due to a lack of management oversight and an immediate need for additional staff to implement the Program, the Department paid for the wages without ensuring that it maintained timesheets for the employee.

Conclusion

The State needs to improve its capacity to effectively and efficiently administer its Program. As previously mentioned, the State lacked adequate procedures and controls to ensure that Program funds would be obligated before the 18-month obligation deadline and were allocated for an eligible project and that it maintained sufficient documentation to support administrative costs, and properly followed Federal requirements.

As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State, and HUD lacked assurance that the State used nearly $8,000 in Program funds for eligible Program administrative costs.

Recommendations

We recommend that the Director of HUD's Chicago Office of Community Planning and Development require the State to

1A. Implement adequate procedures and controls to ensure that it obligates its Program funds for eligible projects before September 4, 2010.

1B. Implement the Authority's plan for the $4,833,000 in Program funds available after the Authority rescinded the Department's allocation to Redevelopment.

1C. Implement adequate procedures and controls to ensure that it awards Program funds for eligible projects and that its recipients use Program funds for the redevelopment of commercial properties in accordance with HUD's requirements.

1D. Provide sufficient supporting documentation or reimburse its Program from non-Federal funds, as appropriate, for the $7,938 in Program funds used for unsupported administrative costs.

1E. Implement adequate procedures and controls to ensure that sufficient documentation is maintained and Program funds are only used for eligible administrative costs.

SCOPE AND METHODOLOGY

To accomplish our objectives, we reviewed

- Applicable laws; the Federal Register, dated October 6, 2008, and June 19, 2009; HUD's regulations at 24 CFR Parts 85 and 570; Office of Management and Budget Circular A-87; HUD's Program grant agreements with the Department and the Authority; HUD's Chicago Office of Community Planning and Development's monitoring report for the State's HOME Investment Partnerships program; HUD's Program policy alert, volume 3, dated April 2010; and the Program's explanation of property types under each eligible use.

- The State's consolidated plan for 2005 and 2010, action plans for 2008 and 2009, annual performance reports for 2007 and 2008, and data from HUD's Disaster Recovery Grants Reporting system.

- The Department's accounting records, policies and procedures, procurement files, contracts and agreements, Program applications, Program distribution and award files, and organizational chart.

- The Authority's audited financial statements, annual reports, accounting records, policies and procedures, contracts and agreements, staffing plans and allocations, job descriptions, organizational chart, and budget.

We also interviewed the Department's and the Authority's employees, Redevelopment's personnel, and HUD's staff.

As previously stated, on March 4, 2009, HUD entered into a grant agreement with the State's Department for more than $53.1 million in Program funds.

We reviewed the State's Program to determine whether the State had the capacity to effectively and efficiently administer its Program.

We reviewed the 18 projects for which the Department allocated nearly $47.3 million in Program funds on September 2, 2009, and the nearly $517,000 in Program funds the Authority set aside as a contingency reserve for the projects to determine whether the State had the capacity to obligate Program funds before the required 18-month obligation deadline and awarded Program funds for eligible projects.

We reviewed all of the State's Program administrative expenses for the period March 2009 through March 2010. The administrative expenses totaled nearly $540,000 and were selected to determine whether the State used Program funds for eligible administrative costs.

We reviewed the 17 grant agreements that the Authority entered into with entities from April 6 through May 20, 2010. The grant agreements totaled nearly $42.5 million in Program funds.

The grant agreements were selected to determine whether the State sufficiently protected Program funds.

We performed our audit work from February through June 2010 at the Department's offices located at 401 South Clinton Street and 100 West Randolph, Chicago, IL; the Authority's office located at 401 North Michigan Avenue, Chicago, IL; and HUD's Chicago, IL, regional office. The audit covered the period July 1, 2008, through December 31, 2009, and was expanded as determined necessary.

We performed our 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 finding and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objectives.

INTERNAL CONTROLS

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

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

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

Relevant Internal Controls

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

- Effectiveness and efficiency of operations - Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

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

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

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness and efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws or regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- The Department and/or the Authority lacked adequate procedures and controls to ensure that Program funds would be obligated before the 18-month obligation deadline and/or that Federal requirements were properly followed in regard to the allocation of Program funds for projects and maintaining sufficient documentation to support Program funds used for administrative expenses.

Separate Communication of a Minor Deficiency

We informed the Authority's executive director and the Director of HUD's Chicago Office of Community Planning and Development of a minor deficiency through a memorandum, dated August 4, 2010.

APPENDIXES

Appendix A

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

Recommendation number	Unsupported 1/	Funds to be put to better use 2/
1B		$4,833,000
1D	$7,938	
Totals	$7,938	$4,833,000

1/ 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.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, if the State implements recommendation 1B, it will ensure that Program funds are spent according to Federal requirements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation | **Auditee Comments**

ILLINOIS HOUSING DEVELOPMENT AUTHORITY

July 16, 2010

Mr. Heath Wolfe
Regional Inspector General for Audit, region V
U.S. Department of Housing and Urban Development
77 West Jackson Blvd, Suite 2646
Chicago IL 60604

RE: Response to the HUD OIG Neighborhood Stabilization Program Audit

Dear Mr. Wolfe:

Enclosed please find a response from the Illinois Housing Development Authority and Illinois Department of Human Services to the HUD Office of Inspector General (HUD OIG) Audit Report on the State of Illinois Neighborhood Stabilization Program. The content of the State's response addresses issues raised in the HUD OIG NSP Draft Audit Report released on June 30, 2010, with certain revisions as proposed by Thomas McManigal of your staff on July 13, 2010.

In particular, Mr. McManigal advised that we should address two portions of the report as if the proposed changes have already been made. These areas included:

Comment 1

- The amount of unsupported administrative costs which would be reduced to $12,947;and

Comment 2

- The removal of the issue (throughout the report) that the Authority did not sufficiently protect Program Funds.

In addition, there were other changes noted by Mr. McManigal. Given that the Draft Audit Report was not finalized, and per our conversation with Brent Bowen today, we are submitting this response with the understanding that it may be necessary to supplement or amend our response depending on the language of the final report.

Thank you.

/signed/
Gloria L. Materre

Ref to OIG Evaluation	Auditee Comments

State of Illinois (State) Response to HUD Office of Inspector General – Neighborhood Stabilization Program Audit Report
Prepared by: Illinois Housing Development Authority and Illinois Department of Human Services
Date: July 16, 2010; supplemented July 27, 2010

General Comments and Response to the HUD Office of Inspector General – Neighborhood Stabilization Program Audit Report – Response Date July 16, 2010; supplemented July 27, 2010

In January 2010, the U.S. Department of Housing and Urban Development Office of Inspector General (HUD OIG) initiated a review of the State of Illinois' capacity to implement the Neighborhood Stabilization Program (NSP) based upon the Congressional identification of the NSP Program as a high risk program, two citizen complaints regarding the prior allocation of NSP program funds and use of administrative funds, and delays in the implementation of the State's NSP activities due to a transfer of administrative responsibilities between agencies of the State. Federal regulations require that all NSP funds be obligated within 18 months of the NSP Grant award to the State.

Comment 3

The HUD OIG staff conducted the audit of the NSP Program for a five month period concurrently with the State's implementation of the NSP Program. The NSP Audit Report recommends that the State improve its capacity to effectively and efficiently administer its Neighborhood Stabilization Program. We appreciate the effort expended by the HUD OIG staff during the review and audit. While the HUD OIG report identified certain specific areas for improvement in the implementation of the NSP Program, we believe that the State has established policies and procedures to effectively implement NSP, and that the specific factors identified by the HUD OIG NSP Audit Report are:

- limited in scope,
- addressed by procedures and documentation in place that were presented to the HUD OIG Auditors, and
- can be further managed through continued procedural improvements.

Comments 4 and 5

The required obligation period for the NSP Program is ongoing at the date of the NSP Audit Report and clear demonstrated progress continues towards the obligation of the full grant by September 4, 2010.

Ref to OIG Evaluation	Auditee Comments
Comments 2 and 3	We believe that the State has demonstrated during the course of the review and audit that the current administrator, the Illinois Housing Development Authority (IHDA), has the staff capacity, experience, and established procedures to implement and protect the NSP Program funds in accordance with the published NSP Program rules and guidelines, and within the mandated timeframes.
	Obligation of Program Funds by September 4, 2010 **HUD OIG Recommendations 1A: Implement adequate procedures and controls to ensure that it [the State] obligates its Program funds for eligible projects before September 4, 2010.**
	The Illinois Housing Development Authority (IHDA) agrees with the recommendation that adequate procedures and controls are necessary in order to ensure that the State can meet the 18 month timeline for fund obligation established for the Neighborhood Stabilization Program in the HERA legislation and HUD Federal Register notice of October 6, 2008. We further agree that the timelines for obligation for funding are constrained for this new and complex federal housing and community development program, and acknowledge the transfer of administrative and program responsibility between State agencies during the grant period has caused a delay in the obligation of NSP funding by the State Grantee and Subgrantees.
Comments 4 and 6	In order to meet the obligation timelines, mitigate the risk of loss of NSP funding through non-obligation of funds, and implement the program in accordance with federal requirements, the Illinois Housing Development Authority (IHDA) has conducted project review and due diligence, established procedures and controls, and instituted project tracking protocols with IL NSP Subgrantees. As of July 16, 2010, over $26.4 million of the total $53.1 million NSP award has been obligated in the HUD NSP reporting system DRGR. As of July 23, 2010, the total obligated NSP funding increased to $31.2 million. Copies of the DRGR Obligation Reports are attached to this Audit response. Continued implementation of established procedures, communication protocols, technical assistance, and project tracking activities will assist Subgrantees to fully obligate funds during the remaining obligation period through September 4, 2010.
	As referenced in the HUD OIG NSP Audit Report, on November 12, 2009, nine months after the initial grant award, the Illinois governor authorized responsibility for implementation of programming for NSP to be transferred from the Illinois Department of Human Services (DHS) to IHDA, the state's housing finance agency. The HUD OIG NSP

Ref to OIG Evaluation	Auditee Comments
	Audit Report acknowledges sufficient staffing capacity and expertise within IHDA to administer the NSP Program.
Comment 5	Since assuming responsibility for NSP, IHDA has moved forward diligently to implement the NSP Program, and appropriately obligate NSP funds in accordance with NSP Program requirements and obligation timelines. The following procedures have been established and activities have been completed: 1) Completed revision of the State of Illinois Substantial Amendment for NSP Action Plan, and entered into the revised NSP Grant Agreement between the US Department of Housing and Urban Development (HUD) and IHDA, on behalf of the State of Illinois. 2) Assigned and trained five full-time and one partially allocated staff within IHDA to assume direct responsibility for the NSP implementation. Roles and responsibilities of direct NSP staff include: project coordination, compliance and reporting, fund draws, and management. Additional IHDA staff work on NSP as needed based upon their specific expertise and assigned responsibilities, i.e. legal counsel prepare documents and oversee project closings; architectural staff review NSP plans and specifications, as applicable for individual projects; financial staff review and approve fund draw requests; and inspectors are assigned to conduct construction inspections in accordance with established procedures. 3) Developed written NSP Program internal procedures based on federal NSP guidance available and incorporating already existing procedures within IHDA for implementing federally funded housing programs. Internal procedures are reviewed periodically based on revised guidance from HUD, and other efficiency improvements identified by NSP staff. 4) Completed project due diligence review of 18 recommended NSP fund allocations forwarded from DHS. NSP Subgrantees proposed a wide range of eligible NSP activities including acquisition and rehabilitation of foreclosed and abandoned homes for sale or rent to low, moderate and middle income households; demolition of blighted properties; redevelopment of an abandoned hotel for housing for homeless veterans; and new construction of multi-unit permanent supportive housing.

Ref to OIG Evaluation	Auditee Comments

5) Drafted and authorized NSP Subgrantee Agreements with 17 Subgrantees. The NSP Agreements define the NSP requirements and obligations of Subgrantees; outline preliminary project parameters, budgets and goals; and set milestones for performance. NSP regulations do not require Subgrantees to include property addresses in the NSP funding agreements. In addition, given the changing availability of foreclosed, abandoned, and REO housing stock targeted for acquisition and rehabilitation under the NSP Program, property specific addresses were not required to be included in the NSP Agreements.

6) Developed the Illinois NSP Subgrantee Manual outlining NSP requirements, procedures, and sample forms to aid Subgrantees to implement their projects under the NSP Program, based on available guidance from HUD as of March 2010.

7) Redesigned and distributed procedure guidance and forms to IL Subgrantees to address updated guidance on eligible property definitions and obligation requirements received from HUD on April 2, 2010 and April 22, 2010, respectively.

8) Implemented and reviewed preliminary Tier I environmental review procedures for all Subgrantees' project areas; with follow up Tier II procedures completed as property addresses are confirmed, and conducted Full Assessment reviews where applicable.

9) Worked with HUD designated NSP Technical Assistance Provider to deliver technical assistance to IL Subgrantees, including assessment of Subgrantee capacity, review of project progress, clarification of technical NSP Program questions posed by Subgrantees, and conduct site visits with those Subgrantees experiencing difficulty with project implementation.

Comment 2

10) IHDA has designed a system to protect NSP Program funds through a series of mechanisms that include legal documents citing NSP Program requirements, review of project closing and all funding draw documentation, escrow agreements outlining final funding commitments, property inspections, and use of third party escrow agents to review and manage all project fund distributions.

Ref to OIG Evaluation	Auditee Comments
	11) Established regular reporting systems with IL NSP Subgrantees on property identification and fund obligation projections. Monthly reports are submitted to HUD CPD on IL NSP Program activities.
Comment 7	12) Developed and implemented an NSP Reallocation Plan to reallocate NSP funds rescinded from previously awarded projects.
Comments 4 and 5	Based on the above completed activities, IHDA has made significant progress towards the obligation deadline for NSP funds. As of July 23, 2010, over $31.2 million of the total $53.1 million dollar NSP grant has been obligated. The above referenced implementation procedures, technical assistance, and project tracking activities will continue to assist Subgrantees to fully obligate funds during the remaining obligation period.
	HUD OIG Recommendation 1B. Implement the Authority's plan for reallocation of the $4,833,000 in Program funds available after the Authority rescinded the DHS allocation to the 55th & State St. Redevelopment Project.
Comment 7	IHDA has moved forward with the implementation of the NSP Reallocation Plan to facilitate obligation of rescinded NSP funding by the September 4, 2010 deadline. As of June 30, 2010, IHDA has reallocated $4.03 million in NSP funding to two projects for eligible program and administrative costs. NSP Subgrantees receiving reallocated funds include 1) an existing IL NSP Subgrantee that has identified all properties for full obligation of an initial $1.3 million NSP award, and has identified additional properties for acquisition and rehabilitation under NSP Eligible Activity B, and 2) an IL NSP Direct Grantee that has obligated over 95% of their initial $5.1 million award, and identified additional properties for acquisition and rehabilitation under Eligible Activity B. An additional award for the balance of NSP resources available for reallocation will be allocated to an existing Subgrantee that has additional funding needs. Proposals were received from current IL NSP Subgrantees requesting additional funding, and other IL NSP Direct Grantees requesting to expand their existing NSP Program. As outlined in the State of Illinois NSP Reallocation Plan reallocation of NSP funding may continue through August 30, 2010.

Ref to OIG Evaluation	**Auditee Comments**
	Project Eligibility **HUD OIG Recommendation 1C. Implement adequate procedures and controls to ensure that it awards Program funds for eligible projects and that its recipients use Program funds for the redevelopment of commercial properties in accordance with HUD's requirements.**
	IHDA has established procedures and controls for review of project activities to determine eligibility under the NSP regulations and guidance. IHDA procedures were designed to review eligibility criteria for all NSP activities not just those proposed under Eligible Activity E – Redevelopment including redevelopment of commercial properties. The established procedures include review of documentation submitted by the Subgrantee once a specific property is identified. Specific criteria reviewed include: 1) location within "area of greatest need" 2) property qualification based on Eligible Activity and National Objective 3) property occupancy status 4) environmental review and clearance 5) purchase price (as applicable) 6) proposed end use, and 7) applicable use restrictions.
	As indicated in the HUD OIG Audit Report, IHDA conducted due diligence on all recommended NSP projects, including the 55th & State Redevelopment Project to ensure that the projects were eligible and would meet HUD's obligation and disbursement requirements. This due diligence review process and other conditions were anticipated and documented in letters sent by DHS to the 55th & State Redevelopment Project and all recommended NSP applicants.
Comment 8	The Authority did not proceed with an award of NSP funds to the 55th & State Redevelopment Project and as such there is no award, nor any expenditure of NSP funding for an ineligible activity. The HUD OIG Audit Report does not accurately reflect the facts concerning the eligibility and due diligence review conducted by the Authority on the 55th & State Redevelopment Project. In a February 9, 2010 letter, the allocation of NSP funds was rescinded from the 55th & State Redevelopment Project based on concerns with the financial feasibility of the project and capacity of the development team to implement within the NSP mandated timeframes. In May 2010, the HUD OIG office made a determination that the property did not meet the vacancy requirements
Comment 9	of Eligible Activity E under the NSP Program. A written definition for vacancy is not included in the NSP regulations or guidance available from HUD.

Ref to OIG Evaluation	Auditee Comments
	HUD OIG Recommendation 1D: Provide sufficient supportive documentation or reimburse its Program from non-Federal funds, as appropriate, for the $12,947 in Program funds used for unsupported administrative costs.
Comment 1	DHS partially agrees with HUD OIG's conclusion that DHS failed to maintain sufficient documentation to support administrative costs relating to a temporary employee and the indirect cost allocation of a vendor. However, the volume of documents produced to HUD OIG, and the content thereof, clearly demonstrates that DHS did, in fact, maintain sufficient documentation to support all administrative costs expended while the Program was administered by DHS.
Comment 10 Comment 1	Throughout the audit, there appeared to be a communication issue with respect to the requests of HUD OIG. However, as HUD OIG's investigation proceeded, HUD OIG's requests for information became more specific and DHS continued to produce documents responsive to each request. DHS produced numerous documents to HUD OIG, and even produced the same documents to HUD OIG on three different occasions. By the time of the July 6, 2010 Exit Conference, the amount of unsupported administrative costs had been reduced to $12,947; this is less than 2.5% of the $539,544 of Program administrative expenses between November 2008 and December 2009.
Comment 1 Comment 11	The temporary employee referenced in the HUD OIG Report was paid $5,625 by DHS. While DHS partially agrees with HUD OIG that adequate documentation was lacking in that the temporary employee did not maintain time sheets, he did work full-time on the Program during his tenure at DHS and prepared an affidavit to that effect. That affidavit has been submitted to HUD OIG. In addition, the affidavit of DHS Assistant Secretary Grace Hou, who was the ultimate supervisor of the temporary employee, was provided to HUD OIG on July 22, 2010, in further support of the fact that the temporary employee worked full-time on the Program. Also on July 22, 2010, in response to questions from one of the auditors as to the calculation of the temporary employee's wages and salary, DHS sent the auditor an e-mail breaking down the calculation of the wages and salary.
Comment 1	With respect to the additional staff, DHS has submitted documentation to HUD OIG, including time sheets and other financial records, to support the calculation of their wages and benefits, most of which HUD OIG has accepted as sufficient documentation to support those administrative costs. In addition, DHS has submitted

Ref to OIG Evaluation	**Auditee Comments**
	documentation to support the disbursements for repaid Program funds, overhead costs, and office expenses.
Comment 1	With respect to support for the repaid Program funds, DHS has provided documentation which it believes supports that disbursement. Following the July 6, 2010 Exit Conference, DHS provided HUD OIG with a copy of a check made payable to the Corporation for Supportive Housing in the amount of $2,438.71. This check, which is dated January 11, 2010 and bears the number AH5903801, represents the balance of the reimbursed funds from the Illinois Assistive Technology Program. The statement in the revised discussion draft audit report that DHS "could not provide documentation to support what it did with the $2,439 of the reimbursed Program funds" is incorrect.
Comment 1	DHS is confident that HUD OIG will conclude that the additional documentation which has been provided is sufficient to support the $12,947 in administrative expenses which are currently in question.
	HUD OIG Recommendation 1E: Implement adequate procedures and controls to ensure that sufficient documentation is maintained and Program funds are only used for eligible administrative costs.
	IHDA has established procedures and controls to ensure that NSP funding is expended for eligible administrative costs, and that documentation is maintained in accordance with federal guidelines. NSP rules and guidelines permit the expenditure of administrative funds to cover NSP related general staffing and management, overhead and indirect costs as well as other NSP costs that cannot be attributed to a specific property. Administrative costs may be incurred by staff or by contracted parties. The systems and procedures put in place by IHDA for NSP are based on established procedures for administration of all grant funding and guidance provided by HUD Technical Assistance Providers.
	General Staffing: NSP funds are invoiced for reimbursement of general staffing and management costs based on completion of electronic time sheets by all IHDA staff; with identifying program codes. The number of hours recorded for the NSP program are then applied to corresponding staff salaries and benefit costs. Documentation is maintained to support the billing to NSP for general staffing and management costs.

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Contract Costs: All contracts for services for the administration of the NSP Program are awarded in accordance with the applicable Federal procurement requirements, State of Illinois Procurement Code and IHDA Procurement Requirements and Procedures. Payments on contracts are approved based on documented completion of the scope of work. Invoices are approved by NSP Program staff and reviewed by managers based on established protocols for payments. Documentation is maintained to support contracts and payment for work completed.

Overhead and Indirect Costs: IHDA implements an indirect cost allocation plan for NSP, HOME and other federal and state funded housing programs. This allocation plan is based on the ratio of recorded hours worked for a specific program to the total hours recorded worked by all IHDA staff. The allocation factor is then applied to general overhead and indirect costs. Documentation is maintained to support the calculation of overhead and indirect cost allocations.

The State Lacked Adequate Procedures and Controls

Comment 3

We disagree with this statement contained in the NSP Audit Report. The language is very broad and does not accurately reflect the conditions and controls that are in place and that were presented to the Auditors. The NSP Audit Report acknowledges that IHDA has:

- put in place sufficient staffing with expertise for implementation of the NSP Program,

Comment 2

- prepared and implemented policies and procedures to implement and protect the NSP Program funds,
- completed due diligence of all recommended projects to determine eligibility and feasibility to meet NSP obligation timelines,
- has rescinded an allocation of $4.8 million in NSP funding to the 55th & State Redevelopment Project ,
- implemented procedures to assure documentation is maintained for use of NSP funds for administrative costs.

Ref to OIG Evaluation	Auditee Comments
Comment 1	Additionally as reported above, DHS has presented documentation to support the use of NSP funds for eligible administrative costs including staffing, overhead, and office expenses.
	Significant Weakness
Comments 3 and 5	We disagree with the conclusion of significant weakness presented by HUD OIG in the NSP Audit Report. Over the course of five months DHS and IHDA presented documentation as noted above in this Response to demonstrate capacity and procedures in place to implement the NSP Program in accordance with published federal regulations and guidance. The Authority continues to work aggressively with Subgrantees to obligate the NSP within the mandated timelines.

OIG's Evaluation of Auditee Comments

Comment 1 We revised this report to state the following:

- The Department lacked sufficient documentation to support that it used $7,938 in Program funds from July through August 2009 for eligible Program administrative costs. The unsupported disbursements included wages for technical assistance personnel ($2,313) and the Department's Program accountant ($5,625).

We removed the following from this report:

- The unsupported disbursements were for technical assistance to community organizations and the State, salaries and benefits, overhead costs, and office expenses.

- In addition, the Department paid Illinois Assistive Technology Project more than $180,000 in Program funds for salaries and benefits and technical assistance, overhead, travel, office expenses, and administrative costs from June through November 2009. In August 2009, Illinois Assistive Technology Project reimbursed the Department $2,670 for unexpended Program funds. However, the Department could not provide documentation to support what it did with $2,439 of the reimbursed Program funds.

- The Department's chief financial officer said that the Department would provide additional documentation to support the disbursements for repaid Program funds, overhead costs, and office expenses.

We also removed from this report the table that showed the cost category and amounts of Program funds paid for the unsupported expenses.

In addition, we amended recommendation 1D to reflect these revisions.

Comment 2 We removed the following from this report:

- The Authority also needs to improve its procedures and controls for protecting Program funds. HUD's regulations at 24 CFR 85.20(b)(3) state that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and ensure that it is used solely for authorized purposes. The Authority entered into grant agreements with two entities for single-site multifamily projects. Although the Authority included a number of provisions in the grant agreements regarding compliance and remedies for noncompliance, it did not fully protect the more than $4.5 million in Program funds for the two projects. It did not ensure that the entities would have sufficient non-Program funds to complete the projects before Program funds could be used.

- The Authority entered into a grant agreement with New Moms for more than $4 million in Program funds. The cost of the project totaled nearly $11.3 million. However, the Authority could not provide firm commitments for more than $6.8 million of the nearly $7.3 million in non-Program funds needed to complete the project. Further, the grant agreement only made the use of the Program funds contingent on New Moms' first receiving and placing into an escrow nearly $6.8 million in non-Program funds needed to complete the project.

- The Authority entered into a grant agreement with Will County, IL, for $500,000 in Program funds. The cost of the project totaled nearly $15.5 million. However, the Authority could not provide firm commitments for any of the nearly $15 million in non-Program funds needed to complete the project. Further, the grant agreement did not include a statement making the Program funds contingent on the non-Program funding from other sources.

We also removed from this report the recommendation that the Director of HUD's Chicago Office of Community Planning and Development require the State to

> Implement adequate procedures and controls to ensure that Program funds are sufficiently protected for single-site multifamily projects that include non-Program funds from other sources. These procedures and controls could consist of including in the State's grant agreements a provision that the receipt and use of the Program funds is contingent on the entities' first receiving all of the non-Program funding from the other sources.

We added to this report that we informed the Authority's executive director and the Director of HUD's Chicago Office of Community Planning and Development of a minor deficiency through a memorandum, dated August 4, 2010.

Comment 3 Although the Authority had sufficient staffing levels and extensive experience with HUD programs, it is at risk of not meeting the required 18-month obligation deadline for Program funds. Further, the Department allocated more than $4.8 million in Program funds for a project that did not comply with HUD's requirements and did not comply with Federal requirements for maintaining sufficient documentation to support the use of nearly $8,000 in Program funds for administrative expenses. These weaknesses occurred because the Department and/or the Authority lacked adequate procedures and controls to ensure that Program funds would be obligated before the 18-month obligation deadline and Federal requirements were properly followed. As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State, and HUD lacked assurance that the State used nearly $8,000 in Program funds for eligible Program administrative costs.

Comment 4 We revised this report to state the following:

- The State needs to improve its capacity to effectively and efficiently administer its Program.

- As of July 23, 2010, the Authority had obligated more than $26.9 million of the State's more than $47.8 million in Program funds set aside for Program projects. As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State.

Comment 5 We agree that the State has made progress in its obligation of Program funds for Program projects. However, of the more than $26.9 million in Program funds the Authority obligated, more than $17.2 million in Program funds (64.1 percent) was for Program projects in which eight entities' proposals identified specific properties for the Program projects and less than $9.7 million in Program funds (35.9 percent) was for Program projects in which nine entities' proposals did not identify specific properties for the Program projects. Further, the Authority had obligated 89.7 percent (more than $17.2 million) of the more than $19.2 million in Program funds it allocated and/or awarded for the Program projects in which the entities' proposals identified specific properties and only 37.3 percent (less than $9.7 million) of the more than $25.9 million in Program funds it allocated and/or awarded for the Program projects in which the entities' proposals did not identify specific properties. As a result, a significant portion of the State's nearly $20.9 million in unobligated Program funds is at risk of being recaptured by HUD and not being used to stabilize neighborhoods and stem the decline in value of neighboring homes in the State, and the State needs to improve its capacity to effectively and efficiently administer its Program.

Comment 6 The State's System report for Program fund obligations, dated July 23, 2010, showed that the Authority obligated more than $31.2 million in Program funds. The obligations included more than $26.9 million for Program projects and more than $4.3 million for administration.

Comment 7 The Authority's commitment to its plan for the more than $4.8 million in Program funds available after it rescinded the Department's allocation to Redevelopment, if fully implemented, should assist the Authority in obligating the more than $4.8 million before September 4, 2010.

Comment 8 We added the following to this report:

- On February 9, 2010, the Authority rescinded the Department's allocation of more than $4.8 million in Program funds to Redevelopment based on concerns with the financial feasibility of the project and Redevelopment's capacity to obligate Program funds within the required 18-month obligation deadline. HUD's Chicago Office of Community Planning and Development asked the Authority to reconsider Redevelopment's proposal due to concerns expressed by community leaders and the need for revitalization in the neighborhood. Therefore, the Authority did not follow through with its February 9, 2010, rescission of the Department's allocation to Redevelopment and continued working with Redevelopment to ensure that Redevelopment would be able to meet HUD's obligation and disbursement requirements for Program funds.

The Authority provided a letter from its executive director to Redevelopment's managing member, dated May 14, 2010, stating that the Authority must rescind the Department's allocation of more than $4.8 million in Program funds to Redevelopment. The executive director stated that HUD's Office of Inspector General raised major concerns as to whether Redevelopment's commercial property was vacant and, therefore, eligible under the Program. The executive director also stated that given the questions regarding the eligibility of Redevelopment's Program project, the Authority could not proceed with awarding the more than $4.8 million in Program funds to Redevelopment. Therefore, the Authority's rescission of the Department's allocation of more than $4.8 million in Program funds to Redevelopment was as a result of our audit.

Comment 9 The Federal Register, dated October 6, 2008, states that eligible uses for Program funds include the redevelopment of demolished or vacant properties. Redevelopment's project would only qualify as an eligible Program project if the entire commercial property was vacant. However, the commercial property was not vacant.

Comment 10 The Department provided many documents to support its administrative costs. However, some of the documentation was insufficient and required additional information and/or documentation to support the administrative costs.

Comment 11 The affidavit of the Department's assistant secretary did not include the number of hours the Department's Program accountant worked. Further, the Department's senior advisor to the secretary stated in his electronic message to us that the Program accountant worked 37.5 hours per week at $25 per hour. The senior advisor also stated that since there were 6 weeks from June 15 through July 31, 2009, the Program accountant's wages totaled $5,625 for the period. However, there were 7 weeks from June 15 through July 31, 2009. Therefore, due to this discrepancy and the Department not being able to provide sufficient documentation to support the number of hours the Program accountant worked during the period, we were unable to determine whether $5,625 in wages for the Program accountant was an eligible administrative expense for the Program.

Appendix C

FEDERAL REQUIREMENTS

Section 2301(c)(1) of Title III of the Act states that any State or unit of general local government that receives amounts pursuant to this section shall, not later than 18 months after receipt of such amounts, use such amounts to purchase and redevelop abandoned and foreclosed-upon homes and residential properties.

The Federal Register, dated October 6, 2008, states that each grantee must use its Program funds within 18 months of HUD signing its Program grant agreement with the grantee. Program funds are used when a State, unit of general local government, or any subrecipient thereof obligates the Program funds for a specific Program activity. Program funds are obligated when orders are placed, contracts are awarded, services are rendered, and similar transactions have occurred that require payment by the State, unit of general local government, or subrecipient. If a State or unit of general local government fails to use its Program funds within 18 months, HUD will recapture any unused funds and reallocate the funds in accordance with 42 United States Code 5306(c)(4).

The Federal Register also states that eligible uses for Program funds include the following: (1) the establishment of financing mechanisms for the purchase and redevelopment of foreclosed-upon homes and residential properties, including such mechanisms as soft-seconds, loan-loss reserves, and shared-equity loans for low- and moderate-income home buyers; (2) the purchase and rehabilitation of homes and residential properties that have been abandoned or foreclosed upon to sell, rent, or redevelop such homes and properties; (3) the establishment of land banks for homes that have been foreclosed upon; (4) the demolition of blighted structures; and (5) the redevelopment of demolished or vacant properties.

In addition, the Federal Register states that except as described in the Federal Register, statutory and regulatory provisions governing the Block Grant program, including the provisions in subparts A, C, D, I, J, K, and O of 24 CFR Part 570, as appropriate, shall apply to the use of Program funds.

HUD's regulations at 24 CFR 85.20(b)(2) require that grantees and subgrantees to maintain records that adequately identify the source and application of funds provided for financially assisted activities. These records must contain information pertaining to grant and subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income. Section 85.20(b)(6) states that accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, and contract and subgrant award documents.

HUD's regulations at 24 CFR 85.22(b) state that allowable costs for State, local, or Indian tribal governments will be determined in accordance with cost principles contained in Office of Management and Budget Circular A-87.

HUD's regulations at 24 CFR 570.502(a) state that recipients that are governmental entities, including public agencies, shall comply with the Office of Management and Budget Circular A-87. Section 570.502(a)(4) states that recipients that are governmental entities shall comply with 24 CFR 85.20, except for section 85.20(a). Section 570.502(a)(6) states that recipients that are governmental entities shall comply with 24 CFR 85.22.

HUD's regulations at 24 CFR 570.506 state that recipients shall establish and maintain sufficient records to enable HUD to determine whether the recipients have met the requirements of 24 CFR Part 570. Section 570.506(a) states that recipients need to maintain records providing a full description of each activity assisted with Block Grant funds; the amount of Block Grant funds budgeted, obligated, and expended for the activities; and the provisions under which the activities are eligible. Section 570.506(h) states that recipients need to maintain financial records in accordance with the applicable requirements in section 570.502. Recipients shall maintain evidence to support how Block Grant funds are expended. The documentation must include invoices, schedules containing comparisons of budgeted amounts and actual expenditures, construction progress schedules signed by appropriate parties, and/or other documentation appropriate to the nature of the activity as applicable.

Attachment A, paragraph C.1, of Office of Management and Budget Circular A-87, revised May 10, 2004, requires all costs to be necessary, reasonable, and adequately documented.

HUD's Program grant agreements with the Department and the Authority, dated March 4, 2009, and December 8, 2009, respectively, state that the following are part of the grant agreements: the Federal Register, dated October 6, 2008; the Act; the State's submission for Program assistance; HUD's regulations at 24 CFR Part 570; and the funding approval.

HUD's Program policy alert, volume 3, dated April 2010, states that HUD generally does not consider Program funds to be obligated for a specific activity unless the obligation can be linked to a specific address and/or household. Program funds are not obligated for an activity when subawards or grants to subrecipients or units of general local government are made.