



Issue Date
September 3, 2010
Audit Report Number
2010-AT-1012

TO: Mary Wilson, Director, Office of Community Planning and Development,  
Knoxville, TN, 4JD

//signed//

FROM: James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: The City of Chattanooga, TN, Needs To Strengthen Controls for Tracking  
Obligations and Reporting for Its Neighborhood Stabilization Program

## **HIGHLIGHTS**

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

We reviewed the City of Chattanooga's (City) Neighborhood Stabilization Program (program). We selected the City for review based on its low percentage of obligations and the approaching September 6, 2010, deadline for obligating funds. Our objective was to determine whether the City administered its program in accordance with U.S. Department of Housing and Urban Development (HUD) rules and regulations.

### **What We Found**

The City generally administered its program in accordance with HUD's rules and regulations. However, it was sometimes inconsistent in identifying obligations and was not always accurate in its reporting to HUD.

## **What We Recommend**

We recommend that the Director of the Knoxville Office of Community Planning and Development continue to monitor the City's progress in obligating its program funds to ensure that it meets the September 6, 2010, deadline. We also recommend that the City be required to develop and implement improved internal controls for tracking obligations and reporting.

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 the draft report to HUD on August 17, 2010, and discussed the report with City officials at an exit conference on August 25, 2010. The City agreed with the report's finding and recommendations.

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

# TABLE OF CONTENTS

---

Background and Objective	4
Results of Audit	
Finding 1: The City Generally Complied With Program Requirements but Some Internal Controls Had Weaknesses	5
Scope and Methodology	8
Internal Controls	9
Appendix A: Auditee Comments and OIG's Evaluation	10

## **BACKGROUND AND OBJECTIVES**

---

The Neighborhood Stabilization Program (program) was authorized under Title III of the Housing and Economic Recovery Act of 2008 (Act). The program provided grants to every State and certain local communities to purchase foreclosed-upon or abandoned homes and to rehabilitate, resell, or redevelop the homes to stabilize neighborhoods and stem declining values in neighboring homes. The Act called for allocating funds “to states and units of the general local government with the greatest need.” In addition, the Act required that not less than 25 percent of the funds be used to benefit individuals or families whose incomes do not exceed 50 percent of area median income. The U.S. Department of Housing and Urban Development (HUD) awarded \$4 billion in grants to 309 grantees. The grantees were allowed 18 months from the date HUD signed their grant agreements to obligate funds and 4 years to expend the funds.

The City of Chattanooga (City) was incorporated under the State of Tennessee Private Acts of 1839. It is governed by a mayor and a nine-member city council. The City received about \$17.2 million in HUD community planning and development funding during the past 3 fiscal years (2008-2010). It received \$2.98 million in program funding including more than \$2.11 million directly from HUD and an additional \$867,625 from the State of Tennessee. The City’s program activities for its \$2.11 million HUD grant include land banks, new construction/redevelopment, demolition, and financing.

<b>Activity</b>	<b>Purpose</b>	<b>Budget</b>	<b>Projected # of units</b>
1- Land banks	Establish land banks for properties that have been foreclosed upon.	\$250,000	5
2- New construction/ redevelopment - vacant units	Redevelop demolished or vacant properties; purchase and redevelop homes and residential properties that have been abandoned or foreclosed upon to sell, rent, or redevelop such homes or properties.	\$1,052,427	17
3- Demolition	Demolish blighted structures that pose a safety hazard to the community.	\$100,000	18
4- Financing	Use program funds to provide principal reductions, interest rate buy-downs, downpayment assistance, and closing costs at zero to low interest rates for qualified home buyers whose incomes do not exceed 120% of area median income.	\$500,000	25
Administration and planning	Use 10% of program funds for administration and planning activities.	\$211,300	NA
<b>Total</b>		<b>\$2,113,727</b>	<b>65</b>

Our objective was to determine whether the City administered its program in accordance with HUD rules and regulations.

## RESULTS OF AUDIT

---

### Finding 1: The City Generally Complied With Program Requirements but Some Internal Controls Had Weaknesses

The City generally complied with program requirements and recently made significant progress in obligating its funds; however, it needs to strengthen its controls over tracking obligations and reporting to HUD. The City's method for tracking obligations was confusing and inconsistent, and its reporting was not always accurate or sufficiently detailed. This deficiency occurred because the City had not developed adequate written procedures for obligation tracking or reporting on its activities. As a result, it lacked assurance that its recorded obligations and reporting to HUD and the public were accurate.

---

#### **The City Generally Complied With Program Requirements**

The City was executing its program in accordance with its approved action plan. With the exception of the internal control weaknesses discussed below, we found no significant deficiencies. The City's planned activities and expenditures were eligible and supported. Although the City had been slow in obligating its funds, it had recently made significant progress in that area.

The regulations require that recipients obligate program funds within 18 months of executing their grant agreements. Thus, the City has until September 6, 2010, to obligate its funds before they become subject to recapture by HUD. As of May 1, 2010, the City had obligated only \$201,300 or about 9.5 percent of its funds. However, during June, it increased its obligations to just over \$1 million or about 49 percent. In addition, the City indicated that it had an additional \$605,680 in pending obligations, potentially bringing its total obligations to more than \$1.6 million or about 78 percent of its funding. If the planned activities are carried out in accordance with the executed project agreements, the City can cover the remaining 22 percent of its outstanding obligations, including the required 25 percent set-aside for families at or below 50 percent of the area median income.

## **The City Needs To Improve Some Internal Controls**

The City needs to improve its procedures for tracking program obligations. Obligations were tracked by the community development manager using a spreadsheet. However, the tracking of obligations was inconsistent, and information on the spreadsheet could not always be traced back to supporting documents. Similar activities on the spreadsheet were treated differently even when they were in the same stage of development. This practice made it difficult for the City to accurately determine and report the obligations. Such inconsistencies could easily result in the City's significantly overstating or understating its obligations.

Grantees are required to submit a detailed quarterly performance report using HUD's Web-based Disaster Recovery Grant Reporting system. The reports must also be posted prominently on the grantee's official Web site.

The City's latest performance report, dated March 31, 2010, understated its obligations by \$29,369 and contained other incorrect information. The City reported obligations of \$201,300, although it had committed to obligations of \$230,669. It failed to include a \$24,000 contract for the rehabilitation of a property located at 113 North Moore Street and understated another contract by \$5,369. The City mentioned the property purchased for rehabilitation in its report narrative but misidentified the property and failed to include the \$24,000 contract as obligated funds.

## **Conclusion**

The City generally complied with program requirements with respect to its program activities and had made significant progress toward obligating its funds. However, it needs to strengthen controls for tracking obligations and reporting. Improved controls will reduce the City's risk of having funding recaptured and improve its reporting to HUD and the public.

## **Recommendations**

We recommend that the Director of the Knoxville Office of Community Planning and Development

- 1A. Continue to monitor the City's progress in obligating program funds to better ensure that the City can obligate its remaining funds before the September 6, 2010, deadline.

- 1B. Require the City to develop acceptable written procedures for improved tracking of obligations and reporting its activities.

## SCOPE AND METHODOLOGY

---

To accomplish our objective, we reviewed

- The program notice, related HUD documents, and the City's program records dated from November 2008 through July 2010;
- 24 CFR (Code of Federal Regulations) 85.12 (special conditions for governmental units), 24 CFR 84.14 (special conditions for nonprofits), and 24 CFR 570.910 (corrective and remedial actions for Community Development Block Grants);
- The City's approved program action plan (submitted to both HUD and the State of Tennessee);
- One hundred percent of the City's claimed program obligations (excluding appraisals and inspections), 100 percent of its program expenditures, and its latest report to HUD; and
- The City's three highest program procurements selected from a total of eight.

All electronic data relied upon during the review were tested during the performance of the various review steps. We found the electronic data to be reliable.

We also interviewed HUD's Knoxville, TN, Office of Community Planning and Development staff and made site visits to a nonstatistical sample of five properties to ensure their **existence**.

We performed our onsite audit work from June 7 through July 2, 2010, at Chattanooga City Hall, 101 East 11<sup>th</sup> Street, Chattanooga, TN.

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



# INTERNAL CONTROLS

---

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

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

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

---

## Relevant Internal Controls

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

- Controls over compliance with laws and regulations.
- Controls over reliability of data.

We assessed the relevant controls identified above.

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

## Significant Deficiencies

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

- Controls over the tracking of program obligations.
- Controls over reporting program activity to HUD.


# APPENDIXES

## Appendix A

### AUDITEE COMMENTS AND OIG'S EVALUATION

#### Ref to OIG Evaluation

#### Auditee Comments



**City of Chattanooga**  
Ron Littlefield, Mayor  
City Hall  
Chattanooga, Tennessee 37402

August 24, 2010

James D. McKay  
Regional Inspector General for Audit  
U.S. Department of Housing and Urban Development  
Region 4 Office of Inspector General  
Office of Audit, Box 42  
Richard B. Russell Federal Building  
75 Spring Street, SW, Room 330  
Atlanta, GA 30303-3388

**SUBJECT:** The City of Chattanooga, TN Needs to Strengthen Controls for Tracking Obligations and Reporting for Its Neighborhood Stabilization Program

Dear Mr. McKay:

I have received your letter regarding the noted subject matter and reviewed it with essential personnel to prepare a response as necessary.

The Draft Audit Report details overall, the City's general compliance with the Neighborhood Stabilization Program requirements but a need to strengthen the controls over tracking obligations and reporting to HUD. In the report, it was recommended that the City be required to develop acceptable written procedures for improved tracking of obligations and reporting activities.

The City of Chattanooga has complied by editing its NSP Policy and Procedure Manual to include detailed guidance on obligating NSP funds, tracking obligations and expenditures and preparing and submitting quarterly reports as required. This information is covered in pages 8-16. Attached are: NSP Policy and Procedures; NSP Obligation & Expenditure Spreadsheet; the latest "Fin Rept7a" extracted from DRGR and an extraction from DRGR's Quarterly Performance Report page, to demonstrate that all reported figures have been reconciled and the latest QPR has submitted.

(423) 425-7800 • FAX: (423) 757-0005 • E-MAIL: mayor@mail.chattanooga.gov

**Comment 1**

City of Chattanooga, TN  
Page 2

**Comment 2**

As shown by the reports, all NSP funds have been obligated and now will be properly tracked. The City also submitted its latest Quarterly Status Report in DRGR prior to the July 31 due date.

I trust that the attached information is sufficient and alleviates any concerns regarding the City's commitment to properly manage the NSP funds.

Sincerely,  
  
Ron Littlefield, Mayor

Enclosures

CC: Beverly P. Johnson  
Sandra Gober

## OIG Evaluation of Auditee Comments

- Comment 1** The City enclosed with its comments proposed changes to its policies and procedures with respect to tracking program obligations and reporting to HUD. If the City implements and follows the proposed changes, more accurate tracking of obligations and reporting to HUD should result. We provided the information to the Knoxville Office of Community Planning and Development for ensuring the changes are implemented.
- Comment 2** The City indicated that it had obligated 100 percent of its program funds. We provided the information to the Knoxville Office of Community Planning and Development.