Office of Community Planning and Development, Washington, DC

Disposition of Real Properties Assisted With Community Development Block Grant Funds

Office of Audit, Region 2
New York – New Jersey

Audit Report Number: 2017-NY-0002
September 29, 2017

To: Stanley A. Gimont, Deputy Assistant Secretary for Grant Programs, DGB

//SIGNED//

From: Kimberly S. Dahl, Regional Inspector General for Audit, 2AGA

Subject: HUD Could Improve Its Controls Over the Disposition of Real Properties Assisted With Community Development Block Grant Funds

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of HUD's oversight of the disposition of properties assisted with Community Development Block Grant funds.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG website. Accordingly, this report will be posted at http://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at 212-264-4174.

Audit Report Number: 2017-NY-0002
Date: September 29, 2017

HUD Could Improve Its Controls Over the Disposition of Real Properties Assisted With Community Development Block Grant Funds

Highlights

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD) oversight of the disposition of real properties assisted with Community Development Block Grant (CDBG) funds. We conducted the audit as part of our annual audit plan. Our audit objective was to determine whether HUD had adequate controls over the disposition of real properties assisted with CDBG funds.

What We Found

HUD could improve its oversight of the disposition of real properties assisted with CDBG funds. Although HUD's drawdown and reporting system allowed grantees to enter identifying information for assisted properties and its field offices performed risk-based monitoring of grantees, HUD's controls were not always sufficient to ensure that grantees (1) entered addresses of assisted properties into its system, (2) provided proper notice to affected citizens before changing the use of assisted properties, (3) adequately determined the fair market value of assisted properties at the time of disposition, and (4) properly reported program income from the disposition of the properties. Further, HUD did not fully implement guidance related to the applicability of change of use requirements after voluntary grant reductions. We attributed these deficiencies to HUD's lack of emphasis on verifying address information, its field office staff not being adequately trained to use data to monitor HUD's interest in properties, and the Milwaukee field office incorrectly interpreting program requirements. As a result, HUD could not track and monitor its interest in the properties and did not have assurance that grantees properly handled changes in use and properly reported program income.

What We Recommend

We recommend that HUD (1) issue guidance reminding grantees of the requirements to report address information for assisted properties and calculate and report program income related to the disposition of these properties; (2) develop a process to ensure that grantees properly report address information and properly calculate and report program income; and (3) require three grantees to provide documentation showing that (a) affected citizens were notified of a change in use of the property for one activity, (b) the fair market value of properties for two activities was supported, and (c) program income for three activities was properly calculated and reported; (4) document the applicability of change of use requirements for one grantee; and (5) issue guidance to clarify the applicability of change of use requirements after voluntary grant reductions.

Table of Contents

Background and Objective 3

Results of Audit 4

Finding : HUD Could Improve Its Controls Over the Disposition of Properties Assisted With CDBG Funds 4

Scope and Methodology 9

Internal Controls 11

Appendixes 12

A. Schedule of Questioned Costs 12

B. Auditee Comments and OIG's Evaluation 13

C. List of Sampled Activities 21

Background and Objective

The Community Development Block Grant (CDBG) program was established by Title 1 of the Housing and Community Development Act of 1974, Public Law 93-383, as amended (42 U.S.C. (United States Code) 530.1). It is one of the U.S. Department of Housing and Urban Development's (HUD) longest continuously running programs. The program provides annual grants on a formula basis to 1,209 States and units of local government to develop viable urban communities by providing decent housing and a suitable living environment and by expanding economic opportunities, principally for low- and moderate-income persons. It is a flexible program that provides communities with resources to address a wide range of unique community development needs. However, to be eligible for funding, every activity must meet one of the following three national objectives: (1) benefit low- and moderate-income persons, (2) aid in preventing or eliminating slums or blight, or (3) address community development having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community for which other funding is not available.

CDBG program funds may be used for several activities, including the acquisition, rehabilitation, demolition, remediation, and improvement of private and public real properties. Over the past 3 years, more than 9 percent of the CDBG funds disbursed went to 13 matrix codes[1] related to activities involving real properties that we identified as higher risk based on prior audit work and a review of matrix code definitions.

Fiscal year	Total program funds disbursed for all matrix codes	Program funds disbursed for 13 matrix codes	Percentage of total
2014	$3,318,992,410	$298,612,167	9.00
2015	3,194,912,077	289,058,315	9.05
2016	3,264,219,590	317,783,537	9.74
Total	**9,778,124,077**	**905,454,019**	**9.26**

These activities often involve large amounts of CDBG funds, are subject to several program requirements related to the use of the properties, and can generate program income upon the disposition of the properties, which can be several years after the funds have been used. Prior audits of grantees located in the State of New Jersey[2] found that grantees did not always protect HUD's interest in the properties and did not always ensure that program income was reported and used for eligible CDBG activities.

Our objective was to determine whether HUD had adequate controls over the disposition of real properties assisted with CDBG funds.

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1 See the Scope and Methodology section for additional details.

2 See 2010-NY-1005, dated December 18, 2009; 2012-NY-1011, dated August 15, 2012; and 2016-NY-1007, dated March 30, 2016.

Results of Audit

Finding: HUD Could Improve Its Controls Over the Disposition of Properties Assisted With CDBG Funds

HUD's Office of Community Planning and Development could improve its oversight of the disposition of real properties assisted with CDBG funds. Although HUD's drawdown and reporting system allowed grantees to enter addresses of assisted properties and its field offices performed risk-based monitoring of grantees, HUD's controls were not always sufficient to ensure that grantees (1) entered addresses of assisted properties into its system, (2) provided proper notice to affected citizens before changing the use of assisted properties, (3) adequately determined the fair market value of assisted properties at the time of disposition, and (4) properly reported program income from the disposition of the properties. Further, HUD did not fully implement guidance related to the applicability of change of use requirements after voluntary grant reductions. We attributed these deficiencies to HUD's lack of emphasis on verifying address information, its field office staff not being adequately trained to use IDIS data to monitor HUD's interest in properties, and the Milwaukee field office incorrectly interpreting program requirements. As a result, HUD could not adequately track and monitor its interest in the properties and did not have assurance that grantees properly handled changes in use and properly reported program income.

HUD Could Improve Its Controls

Although HUD's Integrated Disbursement and Information System[3] (IDIS) allowed grantees to enter addresses of real properties that received CDBG assistance and HUD's field offices performed risk-based monitoring each year, HUD's controls were not sufficient to ensure that grantees provided the information needed to track and monitor its interest in properties assisted with CDBG funds and ensure that grantees properly handled changes in use and reported program income. Further, HUD did not fully implement guidance related to the applicability of change of use requirements.

A review of IDIS data for 588 activities[4] that each received at least $450,000 in CDBG funds between January 2000 and February 2017 found that 220 activities, or 37 percent, had missing, incomplete, or incorrect addresses listed. The CDBG setup detail section of HUD's Guidance for Reporting CDBG Accomplishments and Performance Measures in IDIS required the grantees to enter the address of the activity's physical location into the activity address box and stated that grantees should not use post office boxes or the address of the organization administering the activity in the activity address box. However, some grantees left the address box empty, and others entered post office boxes, subgrantee addresses, or their own addresses instead of the assisted property's address. These deficiencies occurred because HUD did not emphasize the

3 IDIS is the drawdown and reporting system for HUD's Office of Community Planning and Development formula grant programs.

4 The Scope and Methodology section contains additional information related to the 588 activities.

accuracy and completeness of address information for assisted properties. As a result, HUD could not adequately track and monitor its interest in real properties assisted with CDBG funds.

Further, a review of activity files for 10 grantees[5] found significant deficiencies related to three grantees and identified more than $1 million in unsupported costs. The three categories of deficiencies identified are discussed below.

Grantee	Notice of change of use not provided	Fair market value not supported	Program income not properly reported	Unsupported costs
Jersey City	X	X	X	$503,550
Luzerne County[6]		X	X	575,263
Los Angeles County			X	
Totals	**1**	**2**	**3**	**1,078,813**

Affected Citizens Were Not Notified About Change of Use

One grantee (Jersey City, NJ) did not maintain documentation to show that it provided public notice to affected citizens before the disposition of a real property previously assisted with $503,550 in CDBG funds. Regulations at 24 CFR 570.505(a) provide that a recipient may change the use or planned use of an assisted property if the recipient provides affected citizens with reasonable notice of and opportunity to comment on any proposed change. However, Jersey City did not have a public notice or other documentation to show that it had notified affected citizens of the change.

Fair Market Value Was Not Adequately Determined

Two grantees did not adequately determine the fair market value of CDBG-assisted properties before changing the use of the properties. Regulations at 24 CFR 570.505(b) provide that a recipient may change the use or planned use of a CDBG-assisted property if the recipient's CDBG program is reimbursed in the amount of the current fair market value of the property, less any portion of the value attributable to expenditures of non-CDBG funds for acquisition of and improvements to the property. However, Jersey City did not maintain documentation, such as an appraisal report, to support the fair market value of a property that was previously assisted with $503,550 in CDBG funds. Further, Luzerne County determined the fair market value of a property previously assisted with

[5] Appendix C contains additional information related to the 10 grantees reviewed.

[6] This activity received $1,373,536 in CDBG funds. Recommendation 1F addresses the $798,273 incorrectly reported in IDIS and the remaining $575,263 ($1,373,536 - $798,273) is classified as unsupported costs in recommendation 1E because Luzerne County did not provide adequate documentation to support the fair market value of the assisted property at the time of disposition.

almost $1.4 million by using an appraisal report[7] that was 18 months old at the time of disposition and did not represent the fair market value of the property.

Program Income From Disposition Was Not Properly Reported in IDIS

Three grantees did not accurately report program income generated from the disposition of CDBG-assisted properties in IDIS. Chapter 7 of the IDIS training manual pertaining to CDBG entitlement communities provides that when grantees report program income in IDIS, they must use the IDIS ID of the activity that generated the program income. However, Jersey City did not report program income upon the disposition of a real property, although publicly available information showed that program income seemed to have been generated from the disposition,[8] and Luzerne County, PA, and Los Angeles County, CA, reported program income of $798,273 and $300,330 under the wrong IDIS activity IDs.

These deficiencies occurred because HUD's field office staff were not adequately trained to use IDIS data to monitor HUD's interest in properties. While HUD monitored the activities sampled for 4 of the 10 grantees[9] reviewed, its monitoring of the Los Angeles County activity was conducted in 2008, before the County incorrectly reported the program income in 2015. Therefore, HUD could not have detected the issues identified. As a result, HUD did not have assurance that grantees properly handled changes in use and properly calculated and reported program income for the activities related to Jersey City, Luzerne County, and Los Angeles County.

Last, based on discussions with HUD headquarters and Milwaukee field office staff, we determined that HUD did not fully implement the policy set forth in a May 2012 memo related to the applicability of change of use requirements after voluntary grant reductions. Prior to our audit, the State had resolved an eligibility issue by repaying 50 percent of the CDBG funds used for four activities from non-Federal funds and through a voluntary grant reduction for the remaining 50 percent. HUD's Milwaukee field office staff indicated that it considered the four activities to be completely resolved and no longer subject to the change of use requirements because a portion of the funds was repaid. However, the May 2012 memo stated that voluntary grant reductions do not extinguish the applicability of change of use requirements, and HUD did not provide any documentation or written policies to support its claim that the portion of the funds covered by the voluntary grant reduction were no longer subject to the change of use requirements. This occurred because HUD's guidance did not clearly address cases where there was both a repayment from non-Federal funds and a voluntary grant reduction, and because staff

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7 In the February 6, 2015 appraisal report, the appraiser estimated that the market value of the property would increase $420,000 if an additional 4,000 square feet was leased out at $17.50 per square foot beginning June 1, 2015. The space was subsequently leased at that price beginning June 1, 2015. However, when the property was sold on July 29, 2016, the sales price and program income calculation were based on the February 2015 appraised value without the $420,000 increase.

8 The New Jersey County Tax Board Association's website indicates that the property had been sold twice in the past 8 years. It was sold for $325,000 the first time on December 22, 2010, and for $900,000 the second time on January 4, 2017.

9 State of Wisconsin, Los Angeles County, Portland, OR, and Houston, TX

assumed that when a portion of ineligible costs were repaid, it was sufficient to extinguish the applicability of the change of use requirements for the entire activity. As a result, HUD did not have assurance that the grantee would properly handle changes in use and properly calculate and report program income if it later disposes of the property.

Conclusion

HUD could improve its controls over the disposition of real properties assisted with CDBG funds. Because it did not have adequate controls to ensure that grantees entered addresses of assisted properties into IDIS, HUD could not adequately track and monitor its interest in real properties assisted with CDBG funds. For example, HUD could not easily perform a desk review of online sources to determine whether the property had been sold because it did not have the property addresses. Further, because HUD's monitoring did not always occur after grantees changed the use of the properties, HUD did not have assurance that it would detect whether grantees properly determined the fair market value of assisted properties to calculate program income at the time of disposition and whether the program income was properly reported. Last, because HUD did not fully implement guidance related to change of use requirements after voluntary grant reductions, it did not have assurance that a grantee would properly handle changes in use and properly calculate and report program income if it later disposes of the property. If HUD issues additional guidance to its grantees and develops a process to ensure that grantees properly report the addresses of assisted properties and properly calculate and report program income, it can ensure that properties assisted with CDBG funds will be used properly and maximize any further program income, which can then be used for eligible CDBG activities.

Recommendations

We recommend that the Deputy Assistant Secretary for Grant Programs

1A. Issue guidance reminding grantees of the requirement to properly report the addresses of assisted properties in IDIS and properly calculate and report program income from the disposition of these properties.

1B. Develop a process to ensure that grantees properly report the addresses of assisted properties in IDIS and properly calculate and report program income from the disposition of these properties regularly. This process could include but is not limited to developing a process to extract data reported in IDIS on activities with the matrix codes related to real property, and training and instructing the Office of Community Planning and Development's field office staff to extract this data and manually check for address and program income data on grantees' activities, particularly activities that are completed but have properties that could still be subject to program income requirements.

1C. Instruct the Newark, NJ, field office to require Jersey City to provide documentation to show that a notice was provided to affected citizens as required or take action to advise affected citizens that they disposed of the property.

1D. Instruct the Newark, NJ, field office to require Jersey City to provide documentation to support the fair market value of the property at the time of disposition. If documentation cannot be provided, the grantee should be required to reimburse $503,550 to its CDBG line of credit from non-Federal funds. If documentation can be provided, the grantee should be required to determine and reimburse its local bank account from non-Federal funds any additional program income not already reported and properly report the additional program income in IDIS under the activity ID that generated the income.

1E. Instruct the Philadelphia, PA, field office to require Luzerne County to provide documentation to support the fair value of the property at the time of disposition. If documentation cannot be provided, the grantee should be required to reimburse $575,263 to its CDBG line of credit from non-Federal funds. If documentation can be provided, the grantee should be required to determine and reimburse its local bank account from non-Federal funds the additional program income not already reported and properly report the additional program income in IDIS under the activity ID that generated the income.

1F. Instruct the Philadelphia, PA, field office to require Luzerne County to reclassify program income already reported to the activity ID in IDIS that generated the income, ensuring that the $798,273 in program income is properly accounted for.

1G. Instruct the Los Angeles, CA, field office to require the County of Los Angeles to reclassify program income to the activity ID in IDIS that generated the income, ensuring that the $300,330 in program income is properly accounted for.

1H. Instruct the Milwaukee, WI, field office to document that no portion of the four State of Wisconsin's activities reviewed is currently subject to the change of use requirements or remind the State of Wisconsin that the portions of the activities related to the voluntary grant reductions are still subject to the change of use requirements.

1I. Issue guidance to HUD staff and grantees to clarify the applicability of change of use requirements in cases where there is both a repayment from non-Federal funds and a voluntary grant reduction.

Scope and Methodology

We conducted the audit from February through July 2017 at HUD's offices located in Washington, DC, and our office located in Newark, NJ. The audit covered the period January 2000 through February 2017 and was expanded when necessary.

To accomplish our objective, we reviewed

- relevant background information;
- applicable laws, regulations, handbooks, notices, and manuals;
- HUD risk assessments and monitoring reports;
- data contained in IDIS;
- reports from LexisNexis[10]; and
- grantee activity case files.

We also interviewed HUD officials and field office staff located in Washington, DC, Los Angeles, CA, Milwaukee, WI, Newark, NJ, and Philadelphia, PA, to obtain an understanding of its management controls and procedures.

To select a sample of CDBG activities related to acquisition and improvement of real properties for review, we identified 13 matrix codes related to activities involving real properties that we identified as higher risk based on prior audit work and a review of matrix code definitions. The 13 matrix codes included 01 - Acquisition of Real Property, 3D - Youth Centers, 3P - Health Facilities, 3Q - Facilities for Abused and Neglected Children, 3S - Facilities for AIDS Patients, 04 - Clearance and Demolition, 04A - Cleanup of Contaminated Sites, 12 - Construction of Housing, 14B - Rehab: Multi-Unit Residential, 14E - Rehab: Publicly or Privately Owned Commercial/Industrial (CI), 14G - Rehab: Acquisition, 17A - CI: Acquisition/Disposition, and 17C - CI: Building Acquisition, Construction, Rehabilitation. We believe that these matrix codes are for activities that were more likely than others to involve the disposition of real property and generate program income.

We obtained and reviewed IDIS data on all CDBG activities completed, canceled, or open in IDIS during the period January 2000 through February 2017 under the 13 IDIS matrix codes. We identified 3,725 activities that were each funded with $450,000 or more between January 2000 and February 2017. The total funding for these 3,725 activities between January 2000 and February 2017 was $4.3 billion. We sorted the 3,725 activities by each of HUD's 10 regions and

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[10] LexisNexis offers the largest and most comprehensive base of public and proprietary information available today with more than 65 billion records that are refreshed daily. We use this information to help obtain a complete picture of individuals, businesses, and assets.

then selected a sample of 588 activities by applying analytical techniques to the IDIS data for each region. We determined that only 368 of the 588 activities contained address information.

Of the 588 activities, we selected a sample of 13 activities from 10 grantees for review based on the following risk factors identified from our research[11] — a lien or deed restriction did not seem to be imposed on an assisted property, projects were progressing slowly, assisted properties appeared to have been sold, and the CDBG line of credit was not reimbursed for CDBG assistance spent on a canceled activity. The 13 activities from 10 grantees had total funding between January 2000 and February 2017 of $28.4 million and drawdowns totaling $27.2 million. Appendix C contains a list of the 10 grantees and 13 activities reviewed.

We contacted the 10 grantees to obtain the activity case files for the activities selected. Although this approach did not allow us to make a projection to the 3,725 activities that fell under one of the 13 IDIS matrix codes and were funded with at least $450,000 between January 2000 and February 2017, it was sufficient for our purposes. It allowed us to review more documentation related to properties that received $27.2 million and were located in nine of HUD’s 10 regions. While the results of our non-statistical sample can only be applied to the 13 activities reviewed, it allowed us to gain insight into HUD’s controls and identify areas needing improvement.

To achieve our objective, we relied in part on computer-processed data from IDIS and LexisNexis. We used the data to obtain background information and select a sample of activities for review. Although we did not perform a detailed assessment of the reliability of the data, we performed minimal testing and found the data to be accurate for our purposes. Specifically, we reconciled the different sources of data to each other and reviewed source documentation for each of the activities selected for review.

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(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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[11] We used LexisNexis and the New Jersey County Tax Board Association’s website to perform research on the activities that had addresses listed in IDIS.

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 objective:

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- 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.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed the relevant controls identified above.

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

Significant Deficiency

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

- HUD did not have adequate controls to ensure that grantees properly reported the addresses of assisted properties in IDIS and properly calculated and reported program income from the disposition of these properties.

Appendixes

Appendix A

Schedule of Questioned Costs

Recommendation number	Unsupported 1/
1D	$503,550
1E	575,263
Total	**1,078,813**

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.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation | **Auditee Comments**

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-7000

OFFICE OF COMMUNITY PLANNING AND DEVELOPMENT

SEP 2 6 2017

MEMORANDUM FOR: Kimberly S. Dahl, Regional Inspector General for Audit, 2AGA

FROM: Stanley Gimont, Deputy Assistant Secretary for Grant Programs, DG

SUBJECT: Discussion Draft Audit Report – Disposition of Real Properties Assisted with Community Development Block Grant (CDBG) Funds

Summary of HUD Response

Comment 1

HUD appreciates the opportunity to respond to this second, revised draft audit and acknowledges that several changes have been made based on clarifications from HUD. As previous audits have pointed out, problems accounting properly for disposition of Community Development Block Grant CDBG-assisted properties have occurred. HUD does not believe the scale of the problem is as great as OIG suggests, but is not contesting the recommendations.

Comment 2

HUD recognizes that disposition of property acquired and disposed of with CDBG funds has been a somewhat confusing subject for field offices and grantees. HUD has already been developing new guidance to assist grantees and field staff in managing CDBG-assisted property in accordance with applicable requirements.

HUD has placed a CPD Notice in clearance on Management of CDBG-Assisted Property, including a discussion of changes of use. This guidance is currently being amended to address some of the specific issues in the audit that were not in the Notice, particularly on recordkeeping and IDIS. Following publication, HUD plans to present a webinar for field and grantee staff to draw attention to the topic and train program administrators on proper policies and procedures. In addition, HUD has nearly finished a new group of Frequently Asked Questions on acquisition, demolition, and disposition. Together with the Notice, these will give grantee staff the tools they need to understand most situations and the knowledge of where to go for assistance on questions not addressed in the written or PowerPoint training material.

Comment 3

HUD will work with the field offices cited to resolve the deficiencies alleged in the audit, as appropriate. These include the Newark field office for Jersey City, the Philadelphia office for Luzerne County (where HUD has been working for several years to resolve a finding related to property assisted with CDBG funds), and the Los Angeles office for Los Angeles County.

Comment 4

HUD has specific comments below related to some conclusions drawn by OIG. These concern sample size, relative significance of financial findings, and other observations that should be incorporated into the final report. HUD's primary concern is that OIG's choice of matrix codes and over-aggregation of the activities overstates the scale of the problem. Suggesting that over

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Ref to OIG Evaluation	Auditee Comments

Comment 4

9 percent of CDBG expenditures relate to real property management is simply not consistent with program data.

The following section briefly describes how HUD will address the recommendations:

Recommendations

1A. Issue guidance reminding grantees of the requirement to properly report the addresses of assisted properties in IDIS and properly calculate and report program income from the disposition of these properties.

Comment 2

- HUD already has this guidance in development. HUD will modify the clearance draft as appropriate to address this point.

1B. Develop a process to ensure that grantees properly report the addresses of assisted properties in IDIS and properly calculate and report program income from the disposition of these properties regularly. This process could include but is not limited to developing a process to extract data reported in IDIS on activities with the matrix codes related to real property, and training and instructing the Office of Community Planning and Development's field office staff to extract this data and manually check for address and program income data on grantees' activities, particularly activities that are completed but have properties that could still be subject to program income requirements.

Comment 2

- HUD is incorporating these concerns into its Notice on Management of CDBG-Assisted Real Property.

1C. Instruct the Newark, NJ, field office to require Jersey City to provide documentation to show that a notice was provided to affected citizens as required or take action to advise affected citizens that they disposed of the property.

Comment 3

- HUD Headquarters will work with the field office to resolve this recommendation.

1D. Instruct the Newark, NJ, field office to require Jersey City to provide documentation to support the fair market value of the property at the time of disposition. If documentation cannot be provided, the grantee should be required to reimburse $503,550 to its CDBG line of credit from non-Federal funds. If documentation can be provided, the grantee should be required to determine and reimburse its local bank account from non-Federal funds any additional program income not already reported and properly report the additional program income in IDIS under the activity ID that generated the income.

Comment 3

- HUD Headquarters will work with the field office to resolve this recommendation.

Ref to OIG Evaluation	Auditee Comments

1E. Instruct the Philadelphia, PA, field office to require Luzerne County to provide documentation to support the fair value of the property at the time of disposition. If documentation cannot be provided, the grantee should be required to reimburse $575,262 to its CDBG line of credit from non-Federal funds. If documentation can be provided, the grantee should be required to determine and reimburse its local bank account from non-Federal funds the additional program income not already reported and properly report the additional program income in IDIS under the activity ID that generated the income.

Comment 3

- HUD HQ and field office will continue to work with the county to resolve this recommendation by making a revision in IDIS.

1F. Instruct the Philadelphia, PA, field office to require Luzerne County to reclassify program income already reported to the activity ID in IDIS that generated the income, ensuring that the $798,273 in program income is properly accounted for.

Comments 3 and 5

- This need not be a separate finding, as it relates to the same activity in 1 E.

1G. Instruct the Los Angeles, CA, field office to require the County of Los Angeles to reclassify program income to the activity ID in IDIS that generated the income, ensuring that the $300,330 in program income is properly accounted for HUD HQ and field office will continue to work with the county to resolve this finding.

Comment 3

- HUD Headquarters will work with the field office to resolve this recommendation with a revision in IDIS.

1H. Instruct the Milwaukee, WI, field office to document that no portion of the four State of Wisconsin's activities reviewed is currently subject to the change of use requirements or remind the State of Wisconsin that the portions of the activities related to the voluntary grant reductions are still subject to the change of use requirements.

Comment 3

- HUD will work with the Milwaukee office to clarify this matter for the state.

1 I. Issue guidance to HUD staff and grantees to clarify the applicability of change of use requirements in cases where there is both a repayment from non-federal funds and a voluntary grant reduction.

Comment 6

- HUD agrees and will address this relatively rare policy issue in the Notice or FAQs.

HUD Concerns and Recommendations

Comment 7

In the first paragraph of Background and Objectives, the last sentence should read as follows: "(3) or meets other community development needs of a particular urgency that the grantee is unable to finance on its own."

The second paragraph of Background and Objectives states:

Ref to OIG Evaluation	Auditee Comments

"CDBG program funds may be used for several activities, including the acquisition, rehabilitation, demolition, remediation, and improvement of private and public real properties. Over the past 3 years, more than 9 percent of the CDBG funds disbursed went to 13 matrix codes related to activities involving real properties that we identified as higher risk based on prior audit work and a review of matrix code definitions."

Comment 4

HUD disagrees that the nine percent of funds going to these activities is an accurate gauge of the total impact of real-estate transactions. The IDIS matrix codes listed in the Scope and Methodologies section of the audit contain many activities in which the acquisition and disposition of real property is only a minor part, if any, of total costs. The seven activities listed below have limited real property disposition associations; these activities represent over 50 percent of the those cited by the IG as vulnerable. HUD cannot agree with this generalization that conflates total costs with actual costs related to real property disposition. Most of the public facilities, like Youth Centers and Facilities for AIDS patients, involve rehabilitation of existing structures where no acquisition is taking place and structures are rarely sold. Some of them are only disposed of when the grantee or subrecipient is upgrading to a larger or more modern facility. Many of the other codes cited below are either clearance or rehabilitation; HUD's IDIS expert says that little if any of these costs involve acquisition or disposition.

Activities and Matrix Codes where real property disposition is a small percentage of costs: 3D - Youth Centers, 3P - Health Facilities, 3Q - Facilities for Abused and Neglected Children, 3S - Facilities for AIDS Patients, 04 - Clearance and Demolition, 04A - Cleanup of Contaminated Sites, 14E - Rehab: Publicly or Privately Owned Commercial/Industrial (CI).

HUD agrees that some of these activities have costs involving property disposition. However, it is misleading to claim that all costs associated with such activities are property-related. This matters because one might conclude that 9 percent of all expenditures are at risk, a significant figure, when in fact it is more likely less than 5 percent.

Comment 8

HUD also objects to the fact that a majority of the sample activities are at least nine years old. While some may have been sold in this decade, reaching back to the year 2000 makes HUD question the value of the results. At minimum, OIG should define the disposition date.

The second paragraph of the section titled, "HUD could improve its controls" states:

"The CDBG setup detail section of HUD's Guidance for Reporting CDBG Accomplishments and Performance Measures in IDIS required the grantees to enter the address of the activity's physical location into the activity address box and stated that grantees should not use post office boxes or the address of the organization administering the activity in the activity address box."

Comment 9

The audit states that HUD has required grantees to enter addresses; therefore, HUD does have controls in place. Grantees do not always follow the guidance. HUD tries to monitor activities for compliance but has limited staff capacity, and thus cannot monitor every real estate transaction for every grantee. However, HUD already had in clearance both a CPD Notice and a set of Frequently

Ref to OIG Evaluation

Auditee Comments

Asked Questions, to assist field staff and grantees in understanding their responsibilities. HUD has pulled back the Notice to add several clarifying sections to address issues in the audit that were not yet in the guidance.

In the Scope and Methodology section, OIG states:

"We obtained and reviewed IDIS data on all CDBG activities completed, canceled, or open in IDIS during the period January 2000 through February 2017 under the 13 IDIS matrix codes. We identified 3,725 activities that were each funded with $450,000 or more between January 2000 and February 2017. The total funding for these 3,725 activities between January 2000 and February 2017 was $4.3 billion…

"We contacted the 10 grantees to obtain the activity case files for the activities selected. Although this approach did not allow us to make a projection to the 3,725 activities that fell under one of the 13 IDIS matrix codes and were funded with at least $450,000 between January 2000 and February 2017, it was sufficient for our purposes."

Comment 10

This would not have been sufficient for HUD purposes. Thirteen activities of 3,725 is 0.3 percent. This has no statistical validity. Further, of the 13, with $27.2 million in expenditures, there were no disallowed costs and just $1,078,812 in unsupported costs, or 4.0 percent. Four percent unsupported costs in a "sample" that represents 0.3 percent of the universe, yields a meaningless number. The final report should state that these results do not establish that any pattern exists, of abuse or of compliance. In conjunction with the methodological issue of the inapplicability of many of the matrix codes, the OIG should temper any claims of identifying a serious problem.

Also in the Scope and Methodology section, OIG states:

"Of the 588 activities, we selected a sample of 13 activities from 10 grantees for review based on the following risk factors identified from our research: a lien or deed restriction did not seem to be imposed on an assisted property, projects were progressing slowly, assisted properties appeared to have been sold, and the CDBG line of credit was not reimbursed for CDBG assistance spent on a canceled activity."

Comment 11

As we noted in our meeting, there is no statutory or regulatory requirement for liens to be placed on CDBG-assisted properties. Reimbursement for cancelled activities would be to the local account for most of these projects, given their age.

Appendix C is missing a header for the fourth column.

Thank you again for the opportunity to comment on the OIG's draft report. I look forward to our continued engagement on these important issues.

OIG Evaluation of Auditee Comments

Comment 1 HUD indicated that while it does not contest the recommendations, the scale of the problem is not as great as OIG suggests. However, our review of IDIS data for 588 activities found 220 activities, or 37 percent, had missing, incomplete, or incorrect addresses. Further, our review of activities related to ten grantees found that three did not accurately report program income generated from the disposition of properties previously assisted with CDBG funds. While the results of our non-statistical sample can only be applied to the activities reviewed, it was sufficient to show that HUD's controls were not always sufficient to ensure grantees' compliance with CDBG program requirements and can be improved.

Comment 2 HUD acknowledged that the disposition of properties acquired or disposed of with CDBG funds has been a somewhat confusing subject for field offices and grantees, and indicated that it is currently developing written guidance and will modify it to address some of the specific issues in the audit that were not in the Notice, such as recordkeeping and IDIS issues. HUD noted that it will also provide a webinar for field office and grantee staff and is currently developing a frequently asked questions document related to acquisition, demolition, and disposition. These actions are generally responsive to recommendations 1A and 1B. However, we contend that the notice should cover more than the acquisition and disposition of properties. The change of use and property disposition requirements discussed in our report also cover properties that were not acquired with CDBG funds but that used CDBG funds for certain other property related items such as clearance, demolition, cleanup, and rehabilitation. HUD should ensure that its guidance adequately addresses all real properties that are subject to disposition and other change of use requirements.

Comment 3 HUD stated that it would work with its field offices to resolve the issues related to Jersey City, Luzerne County, the State of Wisconsin, and Los Angeles County. HUD further noted that it will work with applicable parties to revise information in IDIS for Luzerne County and Los Angeles County, and will work to clarify the issues surrounding the voluntary grant reduction with the State of Wisconsin. These actions are responsive to recommendations 1C, 1D, 1E, 1F, 1G, and 1H.

Comment 4 HUD expressed concern regarding the matrix codes used to select our sample of activities for review and indicated that suggesting that over 9 percent of CDBG expenditures relate to real property management is not consistent with the data. It later noted for some of the matrix codes used for this report, only a small portion, if any, of the costs for the activities would involve the "acquisition and disposition of real property." It also noted that the facilities related to some matrix codes involve rehabilitation of existing structure where no acquisition is taking place, and that these structures are rarely sold. However, our objective involved the disposition of any real properties assisted with CDBG funds, and was not limited to properties acquired with CDBG funds. According to HUD guidance, CDBG funds allocated to activities that fall under the 13 matrix codes used for this report can only be disbursed for certain activities such as the acquisition, rehabilitation, demolition, remediation, and improvement of private and public real properties. Therefore, we contend that all of the funds for these activities should be related to assistance for real properties. Further, because HUD's IDIS does not specifically track the disposition of properties, we are unable to conclude whether sales and other changes in use are rare. However, even if the disposition of real property assisted with CDBG funds was rare, it is important that HUD have adequate controls in place so that it can track and monitor its interest in these properties and to ensure that grantees properly handle changes in use and properly report program income when sales or other changes in use occur.

Comment 5 HUD noted that recommendation 1F should not be separate from recommendation 1E. However, we will keep the two recommendations separate so that recommendation 1F can be closed if it is completed before recommendation 1E.

Comment 6 HUD agreed that it needs to clarify the applicability of change of use requirements and indicated that it will address this relatively rare policy issue in the Notice or frequently asked questions. Because our review did not focus specifically on this issue, we cannot say how rare or common it is. However, HUD's planned action is responsive to recommendation 1I.

Comment 7 HUD requested that we revise the background section to give a more precise description of the third CDBG national objective. While we did not use the exact language proposed by HUD, we updated this section to align with the language on HUD's website.

Comment 8 HUD expressed concern that the majority of the activities sampled were at least nine years old, but acknowledged that some of the properties may have been sold in this decade. We recognize that the initial funding dates for some of the activities reviewed were older. However, we considered the age of activities to be a risk factor because it means there was more time for there to be an unreported change in use or disposition. HUD indicated that OIG should define the disposition date in its report. Because the data in HUD's IDIS does not capture disposition dates, we were unable to consider this information when selecting our sample. However, note that we identified the disposition date for the Luzerne County activity in footnote 7, and added the disposition dates for the Jersey City activity to footnote 8. Further, while the documentation provided by Los Angeles County did not identify the exact date of disposition of the property reviewed, the disposition occurred in January 2015.

Comment 9 HUD noted that it has controls in place related to the reporting of addresses because it has a requirement in place for grantees. It also acknowledged that grantees do not always follow the requirement, and noted that it cannot monitor every real estate transaction for every grantee. HUD then indicated that it would pull back draft guidance so that it could add clarifying sections to address the issues identified during our audit. HUD's planned actions are responsive to our finding and recommendations.

Comment 10 HUD noted that our sampling methodology would not have been sufficient for its purposes. Specifically, it noted that we reviewed only 0.3 percent of the activities in our sampling universe and that it was not statistically selected, and indicated that we identified unsupported costs for only 4.0 percent of the amount sampled. We did not perform a statistical sample because the data in HUD IDIS was not complete or accurate for our purposes. We added clarifying language to our scope and methodology section to note that while the results of our non-statistical sample can only be applied to the 13 activities reviewed, it allowed us to gain insight into HUD's controls and identify areas needing improvement.

Comment 11 HUD noted that there is no statutory or regulatory requirement for liens to be placed on CDBG-assisted properties. We acknowledge that while HUD's HOME Investment Partnership program requires a lien or deed restriction, its CDBG program does not. However, for sampling purposes, we considered the lack of a lien or deed restriction as a risk factor because grantees may not be tracking these properties as closely or reporting any program income generated.

Appendix C

List of Sampled Activities

HUD region – field office	Grantee (activity ID)	Initial funding date	Amount funded	Amount drawn
1 – Boston	City of Boston (18898)	04/12/2016	$2,750,000	$2,612,499
2 – Newark	Jersey City (1586)	12/19/2008	503,550	503,550
3 – Philadelphia	Luzerne County (3534)	11/15/2006	1,373,536	1,373,536
4 – Birmingham	City of Montgomery (1189)	07/30/2013	1,303,000	834,100
5 – Milwaukee	State of Wisconsin (13673-13676)	04/24/2006	12,323,582	12,323,582
6 – Houston	City of Houston (6367)	06/11/2003	1,730,000	1,730,000
7 – Omaha	City of Des Moines (1755)	09/09/2014	975,178	561,195
9 – Los Angeles	Los Angeles County (5057)	12/12/2000	4,299,223	4,299,223
9 – San Francisco	City of Santa Rosa (449)	2/20/2008	1,478,703	1,478,703
10 – Portland	City of Portland (4952)	05/21/2015	1,689,816	1,520,834
Totals			**28,426,588**	**27,237,222**