



# City of Modesto, CA

## Community Development Block Grant Program

**Office of Audit, Region 9  
Los Angeles, CA**

**Audit Report Number: 2018-LA-1005  
July 3, 2018**





**To:** Kimberly Nash, Director, Office of Community Planning and Development, San Francisco, 9AD

**//SIGNED//**

**From:** Tanya E. Schulze, Regional Inspector General for Audit, 9DGA

**Subject:** The City of Modesto, CA, Did Not Use Community Development Block Grant Funds in Accordance With HUD Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the City of Modesto's Community Development Block Grant program.

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 213-534-2471.



**Audit Report Number: 2018-LA-1005**

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**The City of Modesto, CA Did Not Use Community Development Block Grant Funds in Accordance With HUD Requirements**

## Highlights

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### What We Audited and Why

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We audited the City of Modesto's Community Development Block Grant (CDBG) program. We selected the City based on a hotline complaint (HC-2017-2082) regarding the City's rehabilitation program and the U.S. Department of Housing and Urban Development's (HUD) and the HUD Office of Inspector General's risk assessments. The objective of the audit was to determine whether the City used CDBG funds in accordance with HUD requirements, focusing on its rehabilitation activities.

### What We Found

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The City did not use CDBG funds in accordance with HUD requirements. Specifically, it (1) did not follow HUD's and its own requirements for its rental and homeowner rehabilitation projects, (2) drew CDBG funds in advance, (3) provided false information to HUD, (4) spent HUD funds inefficiently, (5) misclassified some delivery costs, and (6) did not include all recipients in its monitoring plan. These conditions occurred because of the City's desire to show HUD that it was close to meeting timeliness requirements, its disregard for HUD's and its own requirements, its lack of sufficient knowledge and capacity, and the failure of its policies and procedures to ensure that it monitored all of its recipients of CDBG funds. As a result, the City was unable to support that its use of more than \$1.6 million in CDBG funds met HUD requirements, and it improperly used \$257,737 for duplicate costs.

### What We Recommend

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We recommend that the Director of HUD's San Francisco Office of Community Planning and Development require the City to (1) support that its use of more than \$1.6 million in CDBG funds met program requirements or repay the program from non-Federal funds, (2) repay the program \$257,737 for duplicate costs from non-Federal funds, (3) implement policies and procedures to ensure that CDBG funds are used in accordance with program requirements, (4) provide training to its staff to ensure sufficient knowledge of CDBG program requirements, and (5) implement policies and procedures to ensure that it includes all of its CDBG recipients in its monitoring plan and that it selects objective samples.

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# Background and Objective

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The City of Modesto, CA, receives annual Community Development Block Grant (CDBG) entitlement allocation funds from the U.S. Department of Housing and Urban Development (HUD). HUD awards grants to entitlement community grantees to carry out a wide range of community development activities directed toward revitalizing neighborhoods, economic development, and providing improved community facilities and services. Federal regulations at 24 CFR (Code of Federal Regulations) 570.208 require that CDBG funds be used for eligible activities that meet one of the three national objectives:

- provide benefit to low- and moderate-income persons,
- aid in the prevention or elimination of slums or blight, or
- meet a need having a particular urgency.

The City's Community and Economic Development Department is responsible for the administration and oversight of the CDBG program. The City received the following CDBG program funds for its fiscal years 2015 and 2016.

<b>Program year</b>	<b>Amount appropriated</b>
2015: July 1, 2015 – June 30, 2016	\$1,848,449
2016: July 1, 2016 – June 30, 2017	1,871,328
<b>Total CDBG funds</b>	<b>3,719,777</b>

According to 24 CFR 570.902, HUD will review the performance of each entitlement recipient to determine whether each recipient is carrying out its CDBG-assisted activities in a timely manner. The City uses a revolving loan fund for its rehabilitation program. A revolving loan fund is a separate fund, independent of other CDBG program accounts, set up for the purpose of carrying out specific activities. These activities generate payments (program income) to the revolving loan funds for use in carrying out the same types of activities. In the past, HUD did not include the revolving loan fund balance in its calculation of program income for its timeliness test; however, HUD notified the City in February 2017 that revolving loan funds would be considered as program income in its May 2017 test. HUD notified the City in May 2017 that it did not meet the timeliness requirements.

Our audit objective was to determine whether the City used CDBG funds in accordance with HUD requirements, focusing on its rehabilitation activities.

# Results of Audit

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## **Finding: The City Did Not Always Use CDBG Funds in Accordance with HUD's or Its Own Requirements**

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The City did not always use CDBG funds in accordance with HUD's or its own requirements. Specifically, it

- Did not follow HUD's and its own requirements for rental rehabilitation projects.
- Did not follow HUD's and its own procurement requirements for homeowner rehabilitation projects.
- Drew CDBG funds in advance.
- Provided false information to HUD concerning the timeliness of project completion.
- Spent HUD funds inefficiently.
- Misclassified some delivery costs.
- Did not include all of its CDBG recipients in its monitoring plan.

These conditions occurred because of the City's desire to show HUD that it was close to meeting timeliness requirements, its disregard for HUD's and its own requirements, its lack of sufficient program knowledge and capacity to efficiently administer the program, and the failure of its policies and procedures to ensure that it monitored all of its recipients of CDBG funds. As a result, the City was unable to support that more than \$1.6 million in HUD funds met HUD requirements and used \$257,737 in ineligible funds on duplicate costs.

### **The City Did Not Follow HUD's and Its Own Requirements for Rental Rehabilitation Projects**

The City could not support that \$993,880 in CDBG funds used to rehabilitate four multifamily rental properties met HUD requirements. The City partnered with the Housing Authority of the County of Stanislaus (HACS) and the Stanislaus County Affordable Housing Corporation (STANCO) to rehabilitate two properties each for \$592,266 and \$401,614, respectively. The City did not follow HUD's and its own requirements when it rehabilitated the projects. The following table shows that procurement and contracting for all four rental rehabilitation projects did not meet HUD requirements.

Rental rehabilitation project deficiencies					
	HACS project no. 201	HACS project no. 608	STANCO project no. 605	STANCO project no. 901	Total
Independent cost estimate not performed	x	x	x	x	4
Project scope of work not prepared	x	x	x	x	4
Missing environmental review			x	x	2
Environmental review not performed before commitment	x	x			2
Incorrect national objective			x	x	2

Independent Cost Estimates Not Performed and Scopes of Work Not Prepared

The City did not perform independent cost estimates or prepare scopes of work for the four projects. Regulations at 2 CFR Part 200<sup>1</sup> require that the City (1) maintain records sufficient to detail the history of each procurement and (2) perform a cost or price analysis with every procurement and make independent cost estimates before receiving bids or proposals (appendix C). Regulations at 2 CFR 200.403(a) also state that costs must be necessary and reasonable. The City’s Community and Economic Development Department supervisor for HUD programs stated that the City rushed the rehabilitation projects to spend the funds before HUD’s 2017 timeliness test<sup>2</sup> and relied on STANCO and HACS to perform the work and determine whether the costs were reasonable. The City also stated that it did not develop a cost estimate because STANCO

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<sup>1</sup> CFR 200.318(i) and 2 CFR 200.323(a)

<sup>2</sup> Regulations at 24 CFR 570.902 state that HUD will review the performance of each entitlement recipient to determine whether each recipient is carrying out its CDBG-assisted activities in a timely manner. HUD performs the tests 60 days before the end of its current program year.

and HACS were material experts and knew the properties best. Since the City did not perform independent cost estimates or prepare scopes of work, it could not support that \$592,266 spent on the HACS projects and \$401,614 spent on the STACNCO projects were reasonable.

#### Missing Environmental Reviews and Environmental Reviews Performed After Commitment of Funds

The City could not support that it completed environmental reviews of the two STANCO projects, and it completed environmental reviews for the two HACS projects after commitment of funds. Requirements at 24 CFR Part 58<sup>3</sup> state that grantees must maintain a written record of the environmental review and an environmental review must be completed before the commitment of funds (appendix C). The City stated that it completed environmental reviews for all four projects. However, it was unable to provide evidence that it completed environmental reviews for the STANCO projects. For the HACS projects, the City performed environmental reviews after commitment of funds.

#### Incorrect National Objective

The City did not ensure that the two properties rehabilitated by STANCO met one of HUD's CDBG national objectives in accordance with 24 CFR 570.200(a)(2) (appendix C). The STANCO properties were transitional housing, which is considered a public facility, and the reported national objective of low and moderate housing rehabilitation for multiunit residential properties excludes public facilities.<sup>4</sup> The City needs to ensure that it adequately reported and documented that the two STANCO transitional housing properties met one of HUD's national objectives.

#### HUD Funds at Risk Due to Lack of Written Agreements and Advanced Payments

The City put HUD funds at risk because it did not execute written agreements for the four rehabilitation projects<sup>5</sup> and made payments to HACS and STANCO before work was completed. This deficiency violated HUD requirements because at the time of payment, the City had not received any goods or services,<sup>6</sup> and the City's policy was to pay contractors on a reimbursement basis.

These conditions occurred because of the City's desire to show HUD that it was close to meeting timeliness requirements and it disregarded HUD's and its own requirements. As a result of these issues, the City could not support that \$592,266 spent on the HACS projects was reasonable. It also could not support that \$401,614 spent on STANCO projects was reasonable, that its STANCO projects met one of HUD's national objectives, and that its STANCO projects did not have an adverse environmental impact.

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<sup>3</sup> 24 CFR 58.38 and 24 CFR 58.22(a)

<sup>4</sup> Guide to National Objectives and Eligible Activities for Entitlement Communities, Eligible Types of Properties and Public Facilities and Improvements (appendix C)

<sup>5</sup> 24 CFR 570.506(4) (appendix C)

<sup>6</sup> 2 CFR 200.405(a) (appendix C)



## **The City Did Not Comply With HUD's and Its Own Procurement Policies for Homeowner Rehabilitation Projects**

The City did not procure construction services in accordance with HUD's and its own requirements for 10 homeowner rehabilitation projects totaling \$173,508. Specifically, it

- Did not advertise all 10 projects for a sufficient amount of time. HUD requirements for the sealed bid method used by the City state that projects must be advertised to allow for sufficient response time before the date set for opening bids.<sup>7</sup> The City's policies defined sufficient response time as allowing 8 days for a mandatory walkthrough. None of the projects reviewed allowed 8 days for the mandatory walkthrough, and four were advertised for only 1 day before the walkthrough.
- Did not obtain sufficient competition. The City's policies state that it will obtain a minimum of three bids. However, it appeared that the City's limited walkthrough period may have restricted competition because it received fewer than 3 bids on 8 of the 10 projects.
- Potentially restricted competition through various arbitrary actions.<sup>8</sup> Regulations at 2 CFR 200.319(a)(7) state that any arbitrary actions in the procurement process are considered restrictive to competition (appendix C).

These issues occurred because the City disregarded HUD's and its own requirements. As a result, the City could not ensure that costs were reasonable.

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<sup>7</sup> 24 CFR 200.320(c)(2)(i) (appendix C)

<sup>8</sup> Arbitrary actions included (1) awarding one project to a contractor that did not attend the mandatory walkthrough, (2) paying a contractor more than the contract amount without a change order, (3) not following its emergency repair procedures on four projects, and (4) bid opening before the advertised date.

Homeowner rehabilitation project deficiencies			
Property identifier	Days before mandatory walkthrough	Number of bids	Project cost
225	3	1	\$2,883
824	1	2	23,515
933	3	3	29,992
2321	3	1	18,951
3456	1	3	10,000
3931	1	2	4,365
4328 (February contract)	4	2	8,260
4328 (April contract)	7	2	11,840
1421	1	2	50,638
1100	Not advertised	2	13,064
<b>Total</b>			<b>173,508</b>

### **The City Provided False Information to HUD**

The City provided false information to HUD when it drew funds in advance for expenses related to projects that were not complete and made false statements in its communications to HUD. In all, the Community and Economic Development Department drew nearly \$1.3 million in CDBG funds in advance, which gave the appearance to HUD that the City had spent the funds, projects had been completed, and the City was closer to meeting HUD's timeliness requirements. Included in this amount was \$257,737 in ineligible duplicate costs and \$45,304 in homeowner rehabilitation costs for projects that we did not review and may not have met HUD requirements.

Activity	Amount
Advance draw for the STANCO projects <sup>9</sup>	\$361,453
Advance draw for the HACS projects <sup>10</sup>	592,266
Duplicate cost for HACS projects (recommendation 1G)	257,737
Advanced draws for five homeowner rehabilitation projects that did not meet HUD requirements <sup>11</sup>	41,442
Advanced draws for the remaining eight homeowner rehabilitation projects (recommendation 1H)	45,304
<b>Total advanced HUD draws</b>	<b>1,298,202</b>

The City was able to draw the funds in advance because it disregarded HUD's and its own policies when it paid for work that was not complete and because the City's procedures for HUD voucher revisions did not require a second level of approval as did the initial draws. Specifically, the City

- Drew \$361,453 from voucher 6035061 in advance for the STANCO rental rehabilitation projects on April 25, 2017. This amount was equal to the full cost minus the retention amounts of the STANCO rental rehabilitation projects. However, STANCO did not complete the project until June 21, 2017.
- Drew \$592,266 in advance from voucher 6035061 for the HACS rental rehabilitation projects on April 25, 2017, from revolving loan funds. This amount was equal to the full cost minus the retention amount of the HACS rental rehabilitation projects. However, HACS did not complete the project until February 9, 2018.
- Drew an additional \$592,266 in entitlement funds from voucher 6036571 on April 28, 2017, for the same HACS rental rehabilitation project cost.
- Revised the original voucher 6035061 on May 19, 2017. However, the City canceled only a portion of the voucher and left \$257,737 in duplicate expenses. The City later used expenses paid as late as February 9, 2018, to support the nonduplicate portion of the draw.

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<sup>9</sup> This amount was included as unsupported costs related to the STANCO rental rehabilitation projects (recommendation 1C).

<sup>10</sup> This amount was included as unsupported costs related to the HACS rental rehabilitation projects (recommendation 1B).

<sup>11</sup> This amount was included as unsupported costs related to the homeowner rehabilitation program (recommendation 1D).

- Drew \$86,746 in advance for 13 homeowner rehabilitation projects. Five of these projects totaling \$41,442<sup>12</sup> were included in our review, and we determined that the projects did not meet HUD requirements. However, it was unclear whether the remaining eight projects with at least \$45,304 in HUD draws met HUD requirements, including procurement and eligibility.
- Requested advance contractor invoices for some of the homeowner rehabilitation expenses and submitted the invoices to the City's accounting department before the work was completed. The City's accounting department relied on the City's Community and Economic Development Departments' certifications that the work was completed and issued payment. The City stated that it intended to hold the checks until work was completed; however, some contractors cashed the checks shortly after the check issue dates.

The City also made false statements to HUD that did not accurately reflect the activities of its CDBG program. On May 8, 2017, the City told HUD in an email that it did not cancel the full amount of the duplicate draw for the HACS rental rehabilitation project because it had additional eligible activity after the draw date. However, the City did not have sufficient eligible activity to support the entire draw by May 8, 2017. The City also made several false statements in a letter to HUD, dated June 5, 2017. For example, the City stated that

- Although the City did not meet HUD's adjusted timeliness ratio,<sup>13</sup> it did meet the unadjusted timeliness ratio.<sup>14</sup> However, without the homeowner and rental rehabilitation advanced payments from the entitlement fund, the City would not have met the unadjusted ratio.
- It completed the environmental reviews for the rental rehabilitation projects on April 4, 2017. However, the City could not support that it completed the environmental reviews by that date.
- Contracts for the rental rehabilitation projects were executed on April 5, 2017. However, the City did not support that it executed contracts with HACS and STANCO. In addition, HACS and STANCO did not execute agreements with their contractors until after April 5, 2017.

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<sup>12</sup> This amount was included as unsupported costs related to the homeowner rehabilitation program (recommendation 1D).

<sup>13</sup> To meet the adjusted timeliness ratio, the amount of CDBG program income the recipient has on hand, together with the amount of funds in its CDBG line of credit, cannot exceed 1.5 times the entitlement grant amount for its current program year.

<sup>14</sup> To meet the unadjusted timeliness ratio, the amount of entitlement grant funds in its CDBG line of credit cannot exceed 1.5 times the entitlement grant amount for its current program year.

- HACS and STANCO successfully rehabilitated 68 and 24 units, respectively. However, both HACS and STANCO completed their projects after the June 5, 2017, letter. HACS completed its projects on February 9, 2018, and STANCO completed its projects on June 21, 2017.

This condition occurred because of the City's desire to show HUD that it was close to meeting timeliness requirements. As a result, HUD did not have accurate information when determining the appropriate course of action for the City's inability to spend HUD funds in a timely manner.

### **The City Spent HUD Funds Inefficiently and Misclassified Some Delivery Costs**

The City charged the CDBG program for the rehabilitation administration costs (program delivery costs) related to its rehabilitation program. For program year 2015, the City spent \$186,480 on actual homeowner rehabilitation costs and \$323,563 on delivery costs. Therefore, the program delivery costs represented 174 percent of the actual homeowner rehabilitation costs. The delivery costs charged to the program were not reasonable or efficient in proportion to the level of actual rehabilitation costs for work completed as required by HUD regulations at 24 CFR 200.403(a) and 200.404(a) (appendix C). As a result of the City's lack of efficiency in the administration of the rehabilitation program, all \$323,563 in rehabilitation administration expenses for program year 2015 were not supported.

The City misclassified some rehabilitation administration expenses in program year 2016. Office of Community Planning and Development (CPD) Notice 13-07 states that grantees may charge housing rehabilitation administration expenses (delivery costs) separately in HUD's Integrated Disbursement and Information System (IDIS<sup>15</sup>). For other activities, general program administrative expenses are subject to a 20 percent cap. For this reason, grantees must use care in identifying which expenses they treat as rehabilitation administration expenses versus delivery costs. The City charged expenses to the rehabilitation administration delivery activity that were not rehabilitation related. The City did not always support that payroll expenses were rehabilitation related. Specifically, it

- Charged \$69,794 in employee payroll and benefits for City employees who did not work on rehabilitation-related activities.
- Charged \$66,910 in payroll expenses to the rehabilitation delivery activity for its former environmental review specialist, who was incorrectly assigned to the rehabilitation administration cost center.
- Could not provide sufficient support to show that \$13,263 in payroll and benefit expenses was for rehabilitation-related activities.

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<sup>15</sup> IDIS is a nationwide database that provides HUD with current information regarding the program activities underway across the Nation. HUD uses this information to report to Congress and to monitor grantees. IDIS is the drawdown and reporting system for CDBG. Our assessment of the reliability of IDIS was limited to the data sampled, and the data were reconciled with data in City's records. Therefore, we deemed the data sampled to be reliable for the audit conclusion; however, we did not assess the reliability of the systems that generated the data.

- Incorrectly charged \$517 in miscellaneous expenses.<sup>16</sup>

These issues occurred because the City lacked sufficient program knowledge and capacity to properly and efficiently administer the program.

### **The City's Monitoring Procedures Did Not Include All Recipients of Its CDBG Funds**

The City did not ensure that it included all of its recipients of CDBG funds in its monitoring schedule. Requirements at 24 CFR 570.501(b) state that the City is responsible for ensuring that CDBG funds are used in accordance with all program requirements. The use of designated public agencies, subrecipients, or contractors does not relieve the recipient of this responsibility. The City's monitoring efforts and policies and procedures were generally acceptable for its public service subrecipients. However, the City selected only public service subrecipients for monitoring and allowed subrecipients to select which files the City would review. This condition occurred because the City's policies and procedures for monitoring were not sufficient to ensure that it monitored recipients of CDBG funds for compliance with program requirements and that it selected objective samples.

### **Conclusion**

The City did not always follow HUD requirements for rehabilitation projects and rehabilitation administration, did not provide accurate information to HUD, and did not ensure that it included all recipients in its monitoring plan. These conditions occurred because of the City's desire to show HUD that it was close to meeting timeliness requirements, its disregard for HUD's and its own requirements, its lack of sufficient program knowledge and capacity to efficiently administer the program, and the failure of its policies and procedures to ensure that it monitored all of its recipients of CDBG funds. As a result, the City was unable to support that its use of more than \$1.6 million met HUD requirements, drew \$257,737 in ineligible funds for duplicate costs, HUD relied on inaccurate information submitted by the City, and the City could not ensure that all of its recipients of CDBG funds complied with program requirements.

### **Recommendations**

We recommend that the Director of HUD's San Francisco Office of Community Planning and Development require the City to

- 1A. Support that the \$592,266 spent on the HACS rental rehabilitation projects was reasonable or repay the program from non-Federal funds.
- 1B. Support that the \$401,614 spent on STANCO rental rehabilitation projects was reasonable and met one of HUD's national objectives and that it completed an environmental review or repay the program from non-Federal funds.

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<sup>16</sup> Of the \$517, \$303 was for legal services not related to rehabilitation, \$164 was for prorated moving costs for nonrehabilitation employees, and \$50 was for prorated contract administration costs for a nonrehabilitation project.

- 1C. Develop and implement policies to safeguard HUD funds by ensuring that its projects meet national objectives, have a completed environmental review, and have executed agreements for all projects and verify that work is complete before approving payment, including its rental rehabilitation projects.
- 1D. Update policies and procedures to ensure that costs are reasonable, including preparing an independent cost estimate and a detailed scope of work for each project.
- 1E. Support that \$173,508 spent on homeowner rehabilitation project expenses was reasonable or repay the program from non-Federal funds.
- 1F. Update and implement policies and procedures to ensure that all procurements are conducted in a manner that promotes full and open competition and avoids any arbitrary action in the procurement process, including ensuring that contractors are given sufficient time to respond to solicitations.
- 1G. Repay from non-Federal funds \$257,737 from voucher 6035061 for the duplicate draw.
- 1H. Support that \$45,304 drawn in advance met eligibility and procurement requirements and costs were reasonable or repay the unsupported amount from non-Federal funds.
- 1I. Update its policies and procedures to ensure that the City issues payments to vendors and obtains reimbursement from HUD only after the City's Community and Economic Development Department has verified that work is complete.
- 1J. Support that \$323,563 spent on rehabilitation administration charged in program year 2015 costs was reasonable and benefited the City's rehabilitation program or repay the program from non-Federal funds any amount determined to be unreasonable or ineligible.
- 1K. Reclassify \$69,794 in employee payroll and benefits for City employees that did not work on rehabilitation-related activities or repay the program from non-Federal funds.
- 1L. Support that expenses were related to rehabilitation activities for \$66,910 in payroll expenses charged to the rehabilitation delivery expenses activity for its former environmental review specialist or repay the program from non-Federal funds.
- 1M. Support that expenses were related to rehabilitation activities for \$13,263 in unsupported payroll or repay the program from non-Federal funds.
- 1N. Reclassify \$517 in miscellaneous expenses that was incorrectly prorated or repay the program from non-Federal funds.
- 1O. Provide training for its staff to ensure sufficient knowledge of CDBG requirements regarding when to charge delivery costs, including when to charge payroll to rehabilitation administration, versus general administrative costs.
- 1P. Implement policies and procedures to ensure that the City includes all recipients of CDBG funds in its monitoring plan and that it selects objective sample items for monitoring.

# Scope and Methodology

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We performed our audit work at the City of Modesto located at 1010 10<sup>th</sup> Street, Modesto, CA, from October 17, 2017, to April 10, 2018. Our review generally covered the period July 1, 2015, to September 30, 2017.

To accomplish our objective, we performed the following:

- Reviewed HUD regulations and requirements.
- Interviewed appropriate City staff, partners, and contractors.
- Reviewed relevant City policies, procedures, and controls over the program.
- Reviewed HUD monitoring reports.
- Reviewed the City's consolidated plans, consolidated annual performance and evaluation reports, and action plans.
- Reviewed reports from IDIS to obtain CDBG disbursements for the audit period.
- Reviewed relevant drawdowns (vouchers) and supporting documentation for program expenses.
- Reviewed the City's audited financial statements for fiscal year ending 2016.
- Reviewed documentation from the sampled projects, including procurement documentation, subrecipient monitoring, and payroll certifications.
- Performed site visits to a sample of rental rehabilitation properties.

The audit universe for rehabilitation activities included one rental rehabilitation activity totaling \$993,880 and 44 homeowner rehabilitation projects totaling \$528,296 for the period of October 1, 2015, to September 30, 2017. We nonstatistically selected and sampled the \$993,880 rental rehabilitation activity, which we reviewed for national objectives and other HUD requirements, and \$173,508 for 10 homeowner rehabilitation projects, which we reviewed for procurement requirements.

The City drew 12 CDBG vouchers for the housing rehabilitation administration activity totaling \$760,298 for the period October 1, 2015, to September 30, 2017. We chose a nonstatistical sample based on the largest voucher for program year 2016 totaling \$204,692. We reviewed the expenses charged by the City in this voucher to ensure that it documented that expenses were rehabilitation related.

The City entered into agreements with 23 subrecipients for program years 2015 and 2016. We randomly selected a nonstatistical sample of four monitoring files to review.

We cannot project the results of our audit samples to the universe. However, due to the consistent issues with the former environmental specialist's payroll expenses, we questioned all salary expenses not reviewed as unsupported. In addition, because of the lack of efficiency in the administration of the rehabilitation program, we questioned all rehabilitation administration expenses for program year 2015 as unsupported.



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.

# Internal Controls

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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:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- 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.
- 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 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:

- The City lacked controls, including written policies and procedures, to ensure that program activities complied with HUD requirements for its rental rehabilitation projects (finding).
- The City's internal controls were inadequate to ensure that management did not circumvent the policies and procedures in place regarding vendor payments and HUD draws (finding).
- The City lacked the capacity to efficiently administer its CDBG program to ensure that it complied with HUD requirements (finding).
- The City lacked controls, including written policies and procedures, to ensure that it included all of its CDBG recipients in its monitoring plan and selected objective samples when performing its reviews (finding).

# Appendixes

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## Appendix A

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**Schedule of Questioned Costs**

<b>Recommendation number</b>	<b>Ineligible 1/</b>	<b>Unsupported 2/</b>
1A		\$592,266
1B		401,614
1E		173,508
1G	\$257,737	
1H		45,304
1J		323,563
1K		69,794
1L		66,910
1M		13,263
1N		517
<b>Totals</b>	<b>257,737</b>	<b>1,686,739</b>

- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations. In this instance, the \$257,737 in ineligible costs represents a payment for duplicate costs.
- 2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures. In this instance, the unsupported costs represent (1) \$993,880 for the unsupported rental rehabilitation projects, (2) \$173,508 for the

unsupported homeowner rehabilitation project costs, (3) \$45,304 for the unverified advance draws, (4) \$323,563 for the unsupported 2015 rehabilitation administration costs, (5) \$69,794 for the unsupported payroll costs inappropriately charged to the rehabilitation administration activity, (6) \$66,910 for unsupported payroll expenses for the prior environmental review specialist, (7) \$13,263 for other unsupported payroll costs, and (8) \$517 for unsupported miscellaneous expenses.

# Appendix B

## Auditee Comments and OIG's Evaluation

### Ref to OIG Evaluation

### Auditee Comments



City of Modesto  
Office of the City Manager  
1010 Tenth Street, Suite 6100  
Modesto, CA 95354

June 7, 2018

Tanya E. Schulze  
Regional Inspector General for Audit  
U.S. Department of Housing & Urban Development  
Office of Inspector General, Region IX  
300 N. Los Angeles Street Suite 4070  
Los Angeles, CA 90012

*Transmitted via email and U.S. Postal Service*

**Re: City of Modesto OIG Draft Audit Report**

Dear Ms. Schulze:

This letter transmits the City of Modesto's response to the Office of the Inspector General (OIG) Draft Audit Report dated May 23, 2018.

The City of Modesto has carefully reviewed the OIG's findings and recommendations and appreciates the opportunity to provide comments on the OIG Draft Audit Report. Furthermore, we are grateful for the cooperation of the OIG staff in working with the City both during the audit process and in the completion of the Draft Audit Report.

As we understand it, the OIG audit reviewed the City of Modesto's 2017 rehabilitation program, and had some concerns regarding program knowledge and the City's execution of the program as it relates to HUD's requirements.

The City of Modesto has been a HUD entitlement city for over twenty years. During that time it has successfully managed over seventy million dollars in HUD program funding, awarding grants to thousands of programs recipients.

During the audited period and the last several years, the City's HUD team has been restructured. The City's HUD team was moved from the Parks, Recreation and Neighborhoods Department to the Community and Economic Development Department. Since that move, key positions (which had been vacant for extended periods of time) were filled and will continue to be filled. There are now newly developed process flows, new policies and procedures, and training that will continue on an ongoing basis. The City has done much in the last few months to gain higher performance standards.

P.O. Box 642, Modesto, CA 95353

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Phone: (209) 577-5223 • Fax: (209) 571-5128

Comment 1

The City has reviewed all of the findings from the OIG, and is working diligently to address the concerns. An outline of the City responses is set forth below.

**OIG Finding 1A and 1B: Support the funding spent on Rental Rehabilitation Projects**

All projects funded and completed by the City of Modesto during the audit period aligned with an applicable CFR and met a national objective. As the OIG correctly noted for one of the properties, the facilities rehabilitated are "public facilities" (community centers) aimed at the housing needs of persons with a mental health condition. HUD identifies these persons as "persons with special needs." These public facilities (such as group homes or homeless shelters) are examples of facilities that qualify under the Limited Clientele criteria and the populations served by these facilities are presumed to be LMI persons or families.

The City has updated its policies and created the attached "Project Application Proposal Form". This form is now required from all contractors and subrecipients to make sure that the project meets national objectives. Furthermore, all City and HUD required information and data are now collected before a project is considered for funding. This includes the detailed scope of work, the independent cost estimate, the sources and uses, and the timeline for the project. Please see Exhibit 4.

The City will work directly with HUD to provide the scope of work, independent cost estimates, written agreements, and environmental review to remedy the recommendation.

**OIG Finding 1C: Develop and implement policies to safeguard HUD funds by ensuring that its projects meet national objectives, have a completed environmental review, have executed agreements for all projects, and have verified that work is complete before approving payment including its rental rehabilitation projects.**

The City of Modesto HUD Division has been working diligently to implement policies, process flows and checklists to ensure that all projects meet national objectives and follow both HUD and City of Modesto Policies.

Staff has developed the process flows which include staff responsibilities, sign-off and the entry of dates at each step, and supervisor review and approval throughout the process. Please see Exhibit 5. Checklists of information that will be included when executing agreements (exhibit 2), encumbering funds (Exhibit 2), and approving payments (Exhibit 3) have been established.

For example, the City is now using the HUD Environmental Review Online System (HEROS) to ensure all documents are consistent and easy to track. They are uploaded into the system, with executed signature pages, for review and comment by HUD at any point in time.

The attached "Project Application Proposal Form" (Exhibit 4) will be closely adhered to and utilized as a checklist of information to be obtained from the developer, and/or subrecipient

Comment 2

Comment 3

Comment 3

before a project is considered for funding. This will ensure that the City will have the project information, the national objective, scope of work, and independent cost estimate in the file before the project is considered for approval by the Citizen's Housing and Community Development Committee and subsequently by City Council.

Additionally, to ensure project eligibility, Staff has reached out directly to their HUD Representative to obtain feedback on upcoming projects and to confirm that they meet the national objective for the funding stream. The City's HUD representatives have sent several resources that the City intends to closely adhere to, including, "Developing and Implementing a CDBG Workout Plan" and "Guide to National Objectives and Eligible Activities". These resources have been very helpful in reviewing potential projects to ensure they are meeting the national objectives, as well as the needs of the community.

**OIG Finding 1D: Update policies and procedures to ensure that costs are reasonable, including preparing an independent cost estimate and detailed scope of work for each project.**

Staff has made updates to the City- Housing and Urban Development Policies and Procedures to reestablish a policy to ensure that costs are reasonable and include an independent cost estimate and detailed scope of work for each project. This policy is attached for your review, and has been approved by the Citizen's Housing and Community Development Committee on May 10, 2018. It will go to City Council on June 12, 2018 for approval, (Exhibit 6).

Comment 4

Staff is also implementing the attached "Project Application Proposal Form" (as outlined in Chapter 2 -2.3.7 – Project Application Process – CDBG Handbook) to send to contractors and subrecipients to ensure that the project meets a national objective and that all of the required City and HUD information and documentation is collected before a project is considered for funding.

**OIG Finding 1E: Support that \$173,503 spent on homeowner rehabilitation project expenses was reasonable or repay the program from non-Federal funds.**

The City of Modesto has a critical need for funding to rehabilitate the aging affordable housing stock. All of the homeowner rehabilitation projects were utilized to rehabilitate single family units and met the national objective of low mod housing activities (24 CFR 570.208(a) (3)). Approximately 15,000 housing units require rehabilitation (See pg. #2-51, City of Modesto Housing Element).

Comment 5

Staff is working in partnership with the City's Procurement Division to update the Housing and Urban Development Policies and Procedures and to develop steps that will ensure that all procurements are conducted in a manner that promotes full and open competition and avoids arbitrary actions in the procurement process. These new policies and procedures will enable the City to ensure that contractors are given sufficient time to respond to solicitations. The new policy will align with the City of Modesto's own procurement policies, Municipal Code, and HUD Program Policies.



Comment 5

**OIG Finding 1F: Update and implement policies and procedures to ensure that all procurements are conducted in a manner that promotes full and open competition and avoids any arbitrary action in the procurement process, including ensuring that contractors are given sufficient time to respond to solicitations.**

See Item 1E.

**OIG Find 1G: Repay from non-Federal funds \$257,737 from voucher 6035061 for the duplicate draw.**

The City had documentation supporting the initial draw requested from the revolving loan fund for voucher 6035061. When the voucher was revised and its supporting documentation moved to the entitlement general fund from the revolving loan fund, a net difference resulted. Pending projects were reviewed by staff to determine if the City was likely to receive sufficient invoices by April 30, 2017 to justify the remaining balance of \$257,737. Based on an internal project management worksheet that outlines approved projects, pending agreements, and project deliverables, staff was confident that invoices would be processed timely; therefore this amount was not cancelled.

Comment 6

The City's staff continued to monitor projects and spending to ensure there was sufficient backup to offset the draw and a sufficient number of paid invoices to support the overdraw. No revolving loan fund draws were made once it was discovered there were not enough backup invoices to support the overdraw. In January 2018, the City added the total additional invoices needed to support the draw from the revolving loan fund. The first draw the City completed for Program Year 17/18 with revolving loan funds was on April 19, 2018 in the amount of \$21,005.

We thank the OIG for the recent meeting and clarification of the "duplicate draw" deficiency. As a result of this clarification, the City is committed to working directly with its HUD representatives to implement the proposed recommendation.

**OIG Finding 1H: Support that the \$45,304 drawn in advance met eligibility and procurement requirements and costs were reasonable or repay the unsupported amount from non-Federal funds.**

See Item 1E

Comment 5

**OIG Finding 1I: Update its policies and procedures to ensure that the City issues payments to vendors and obtains reimbursement from HUD only after the City's Community and Economic Development Department has verified that work is complete.**

The City's Community and Economic Development Department has implemented an invoice checklist of items that need to be included for an invoice to be processed by the City's Finance Department. This includes a property inspection report reflecting a "pass" for the invoiced work.

Comment 7

Staff is currently updating its policies and procedures to outline this process and to ensure that the City issues payments to vendors and obtains reimbursement from HUD *only after the work is verified* as complete. Payment will not be processed by the City's Finance Department without a completed checklist.

**OIG Finding 1J-IO: Support and reclassify miscellaneous expenses and provide payroll training.**

Staff reviewed the backup documentation for payroll and benefits for City employees. The correct funding source has been identified for each project. Staff is working in partnership with the Modesto Finance Department to reclassify these funds to an eligible funding source to address the OIG's finding.

For Program Year 2018-2019, the housing staff is working directly with the City's Finance department to reclassify and reorganize the budget/accounting structure of the housing division. A single new fund and cost center was created for all staff working on HUD projects, (known as the HUD Administration Fund). Staff time will be charged directly to each grant, based on the activity. This will ensure that no ineligible payroll costs will ever be charged to grants. Staff will utilize a Caltrans-approved indirect rate to capture the full costs associated with each project. HUD has already approved the indirect rate, and staff will solicit HUD's approval of the City's use of this procedure going forward.

The City has reviewed CPD 13-07 to gain a better understanding of Program Administration Costs and Activity Delivery Costs. City staff is working closely with the Finance Department to implement "Program Codes" on time sheets so that they reflect the duties completed during the relevant time period. The City developed this method of identification for all of the departments which utilize Caltrans funding, and is now aligning the methodology with its HUD-funded divisions.

Staff training is occurring in a divisional meeting twice a month to ensure the new policies and payroll structure is implemented. The housing division is reviewing the new internal excel spreadsheet system and attempting to determine how the new system links with the City's payroll system. All time sheets will be regularly reviewed by staff, the Supervisor, and the Department's Manager to ensure staff is implementing the new changes and policies.

**OIG Finding IP: Implement policies and procedures to ensure that the City includes all recipients of CDBG funding in its monitoring plan and that it selects objective sample items for monitoring.**

Staff has updated the Housing and Urban Development Policies and Procedures, which includes a policy to ensure the City conducts monitoring of all subrecipients and selects objective sample items for monitoring. Staff has already implemented this new policy into its current subrecipient monitoring.

The City's Housing and Urban Development Policies and Procedures Manual has been updated to reflect the new policy to ensure the City follows a valid monitoring plan for its recipients and that it selects objective sample items for monitoring in the future. The policy

Comment 8

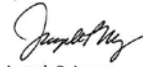
Comment 9

City of Modesto OIG Draft Audit Report  
June 7, 2018  
Page 6 of 6

is attached for your review. The policy was approved by the Citizen's Housing and Community Development Committee on May 10, 2018 and will go to City Council on June 12, 2018 for approval, (Exhibit 7).

Thank you again for the opportunity to provide comments on the Draft Audit Report. Please let us know if you have any questions.

Sincerely,



Joseph P. Lopez  
City Manager

Enclosures:

- Exhibit 1 - Agreement Checklist
- Exhibit 2 - Encumbrance Checklist
- Exhibit 3 - Invoice Checklist
- Exhibit 4 - Project Application Proposal Form
- Exhibit 5 - Housing Rehabilitation Process Flow
- Exhibit 6 - HUD Policies and Procedures – Cost Reasonableness and Detailed Scope of Work
- Exhibit 7 - HUD Policies and Procedures- Objective samples when monitoring subrecipients

cc: Ted Brandvold, Mayor  
Adam U. Lindgren, City Attorney  
Monica Houston, City Auditor

Comment 10

## OIG Evaluation of Auditee Comments

- Comment 1 We acknowledge the changes and vacancies in the department created challenges and we recognize the City's commitment to improving its processes, policies, and procedures.
- Comment 2 We disagree that all rental rehabilitation projects funded and completed by the City met a national objective. As stated in the audit report, the STANCO projects did not meet the reported objective because the projects were transitional housing, which is considered a public facility. The reported national objective of low and moderate housing rehabilitation for multiunit residential properties excludes public facilities such as transitional housing. We acknowledge that the projects may be eligible under a different national objective. The City can work with HUD to identify an eligible national objective for the STANCO projects.
- We commend the City's actions to address the issues identified in the report, including updating its policies to ensure future projects meet national objectives and costs are reasonable. We also commend the City for its commitment to work with HUD to address the issues identified during the audit.
- Comment 3 We commend the City's efforts to implement policies, process flows, and checklists to ensure its projects meet national objectives, have a completed environmental review and executed agreements, and work is complete before payment is issued. The City can work with HUD during the audit resolution process to provide support that the proposed policies and procedures have been approved and implemented.
- Comment 4 We commend the City's commitment in taking the steps necessary to ensure costs are reasonable. The City can work with HUD during the audit resolution process to provide support that the proposed policies and procedures have been approved and implemented.
- Comment 5 We acknowledge that the City's homeowner rehabilitation projects met a national objective. We also acknowledge the City's efforts to update its policies and procedures to ensure its procurements are conducted in a manner that promotes full and open competition. The City can provide the approved policies and procedures to HUD during the audit resolution process.
- Comment 6 We recognize that the City believed there were sufficient invoices to support the duplicate draw. However, it appears unlikely the City had sufficient invoices to support the draw because at the time of the draw, the City was requesting invoices in advance for projects that were not completed. It was also not able to fully support the draw until January 2018. The City will work with HUD during the audit resolution process to ensure it recognizes expenses in the program year in which the expenses occurred and repay all duplicate costs that were drawn in advance.

- Comment 7 We commend the City's commitment in taking the steps necessary to ensure work is complete before requesting reimbursement from HUD. The City will work with HUD during the audit resolution process to provide support that the proposed policies and procedures have been approved and implemented.
- Comment 8 We appreciate the City's efforts to identify the correct funding source for the questioned expenses and modify its budget accounting structure, and its commitment to provide training to employees to ensure only eligible expenses are charged to the rehabilitation administration activity. The City will work with HUD during the audit resolution process to provide support that the proposed policies and procedures have been approved and implemented along with its training program.
- Comment 9 We commend the City's quick action to implement procedures to ensure it does not allow subrecipients to select which files are reviewed and its efforts to update policies and procedures to ensure it monitors all recipients of CDBG funds. The City will work with HUD during the audit resolution process to provide support that its policies and procedures have been approved and implemented.
- Comment 10 The City provided attachments with its response. We did not include the attachments in the report because they were too voluminous; however, they are available upon request.

## Appendix C

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### Criteria

#### **24 CFR 58.22(a)**

Neither a recipient nor any participant in the development process, including public or private nonprofit or for-profit entities, or any of their contractors, may commit HUD assistance under a program listed in Sec. 58.1(b) on an activity or project until HUD or the state has approved the recipient's RROF and the related certification from the responsible entity. In addition, until the RROF and the related certification have been approved, neither a recipient nor any participant in the development process may commit non-HUD funds on or undertake an activity or project under a program listed in Sec. 58.1(b) if the activity or project would have an adverse environmental impact or limit the choice of reasonable alternatives.

#### **24 CFR 58.38**

The responsible entity must maintain a written record of the environmental review undertaken under this part for each project. This document will be designated the "Environmental Review Record" (ERR) and shall be available for public review.

#### **24 CFR 570.200(a)(2)**

Compliance with national objectives. Grant recipients under the Entitlement and HUD-administered Small Cities programs and recipients of insular area funds under section 106 of the Act must certify that their projected use of funds has been developed so as to give maximum feasible priority to activities which will carry out one of the national objectives of benefit to low- and moderate-income families or aid in the prevention or elimination of slums or blight. The projected use of funds may also include activities that the recipient certifies are designed to meet other community development needs having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community where other financial resources are not available to meet such needs. Consistent with the foregoing, each recipient under the Entitlement or HUD-administered Small Cities programs, and each recipient of insular area funds under section 106 of the Act must ensure and maintain evidence that each of its activities assisted with CDBG funds meets one of the three national objectives as contained in its certification. Criteria for determining whether an activity addresses one or more of these objectives are found in §570.208.

#### **24 CFR 570.200(a)(4)**

Compliance with environmental review procedures. The environmental review procedures set forth at 24 CFR part 58 must be completed for each activity (or project as defined in 24 CFR part 58), as applicable.

#### **24 CFR 570.202**

(b) Types of assistance. CDBG funds may be used to finance the following types of rehabilitation activities, and related costs, either singly, or in combination, through the

use of grants, loans, loan guarantees, interest supplements, or other means for buildings and improvements described in paragraph (a) of this section, except that rehabilitation of commercial or industrial buildings is limited as described in paragraph (a)(3) of this section.

(9) Rehabilitation services, such as rehabilitation counseling, energy auditing, preparation of work specifications, loan processing, inspections, and other services related to assisting owners, tenants, contractors, and other entities, participating or seeking to participate in rehabilitation activities authorized under this section, under section 312 of the Housing Act of 1964, as amended, under section 810 of the Act, or under section 17 of the United States Housing Act of 1937;

#### **24 CFR 570.501(b)**

The recipient is responsible for ensuring that CDBG funds are used in accordance with all program requirements. The use of designated public agencies, subrecipients, or contractors does not relieve the recipient of this responsibility.

#### **24 CFR 570.503(a)**

Before disbursing any CDBG funds to a subrecipient, the recipient shall sign a written agreement with the subrecipient. The agreement shall remain in effect during any period that the subrecipient has control over CDBG funds, including program income. At a minimum, the written agreement with the subrecipient shall include provisions concerning the statement of work, records and reports, program income, and uniform requirements.

#### **24 CFR 570.506**

Records to be maintained:

Each recipient shall establish and maintain sufficient records to enable the Secretary to determine whether the recipient has met the requirements of this part. At a minimum, the following records are needed:

(a) Records providing a full description of each activity assisted (or being assisted) with CDBG funds, including its location (if the activity has a geographical locus), the amount of CDBG funds budgeted, obligated and expended for the activity, and the provision in subpart C under which it is eligible.

(4) For each activity carried out for the purpose of providing or improving housing which is determined to benefit low and moderate income persons: (i) A copy of a written agreement with each landlord or developer receiving CDBG assistance indicating the total number of dwelling units in each multifamily structure assisted and the number of those units which will be occupied by low and moderate income households after assistance; (ii) The total cost of the activity, including both CDBG and non-CDBG funds. (iii) For each unit occupied by a low and moderate income household, the size and income of the household; (iv) For rental housing only:

- (A) The rent charged (or to be charged) after assistance for each dwelling unit in each structure assisted; and
- (B) Such information as necessary to show the affordability of units occupied (or to be occupied) by low and moderate income households pursuant to criteria established and made public by the recipient;

**24 CFR 570.902**

HUD will review the performance of each entitlement, HUD-administered small cities, and Insular Areas recipient to determine whether each recipient is carrying out its CDBG-assisted activities in a timely manner.

(a) Entitlement recipients and Non-entitlement CDBG grantees in Hawaii. (1) Before the funding of the next annual grant and absent contrary evidence satisfactory to HUD, HUD will consider an entitlement recipient or a non-entitlement CDBG grantee in Hawaii to be failing to carry out its CDBG activities in a timely manner if:

(i) Sixty days prior to the end of the grantee's current program year, the amount of entitlement grant funds available to the recipient under grant agreements but undisbursed by the U.S. Treasury is more than 1.5 times the entitlement grant amount for its current program year; and

(ii) The grantee fails to demonstrate to HUD's satisfaction that the lack of timeliness has resulted from factors beyond the grantee's reasonable control.

(2) Notwithstanding that the amount of funds in the line of credit indicates that the recipient is carrying out its activities in a timely manner pursuant to paragraph (a)(1) of his section, HUD may determine that the recipient is not carrying out its activities in a timely manner if:

(i) The amount of CDBG program income the recipient has on hand 60 days prior to the end of its current program year, together with the amount of funds in its CDBG line of credit, exceeds 1.5 times the entitlement grant amount for its current program year; and

(ii) The grantee fails to demonstrate to HUD's satisfaction that the lack of timeliness has resulted from factors beyond the grantee's reasonable control.

**2 CFR 200.318(i)**

The non-Federal entity must maintain records sufficient to detail the history of procurement. These records will include, but are not necessarily limited to the following: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

**2 CFR 200.319(a)(7)**

Any arbitrary action in the procurement process are considered restrictive to competition.

**2 CFR 200.320(c)(2)(i)**

The invitation for bids will be publicly advertised and bids must be solicited from an adequate number of known suppliers, providing them sufficient response time prior to the date set for opening the bids.



**2 CFR 200.320(f)**

Procurement by noncompetitive proposals is procurement through solicitation of a proposal from only one source and may be used only when one or more of the following circumstances apply:

- (1) The item is available only from a single source;
- (2) The public exigency or emergency for the requirement will not permit a delay resulting from competitive solicitation;
- (3) The Federal awarding agency or pass-through entity expressly authorizes noncompetitive proposals in response to a written request from the non-Federal entity; or
- (4) After solicitation of a number of sources, competition is determined inadequate.

**2 CFR 200.323(a)**

The non-Federal entity must perform a cost or price analysis in connection with every procurement action in excess of the Simplified Acquisition Threshold including contract modifications. The method and degree of analysis is dependent on the facts surrounding the particular procurement situation, but as a starting point, the non-Federal entity must make independent estimates before receiving bids or proposals.

**2 CFR 200.403(a)**

Costs must be necessary and reasonable for the performance of the Federal award and be allocable thereto under these principles.

**2 CFR 200.404(a)**

A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The question of reasonableness is particularly important when the non-Federal entity is predominantly federally-funded. In determining reasonableness of a given cost, consideration must be given to:

- (a) Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the non-Federal entity or the proper and efficient performance of the Federal award.

**2 CFR 200.405(a)**

A cost is allocable to a particular Federal award or other cost objective if the goods or services involved are chargeable or assignable to that Federal award or cost objective in accordance with relative benefits received.

**2 CFR 200.415(a)**

To assure that expenditures are proper and in accordance with the terms and conditions of the Federal award and approved project budgets, the annual and final fiscal reports or vouchers requesting payment under the agreements must include a certification, signed by an official who is authorized to legally bind the non-Federal entity, which reads as follows: "By signing this report, I certify to the best of my knowledge and belief that the report is true, complete, and accurate, and the expenditures, disbursements and cash receipts are for the purposes and objectives set forth in the terms and conditions of the

Federal award. I am aware that any false, fictitious, or fraudulent information, or the omission of any material fact, may subject me to criminal, civil or administrative penalties for fraud, false statements, false claims or otherwise.(U.S. Code Title 18, Section 1001 and Title 31, Sections 3729–3730 and 3801–3812).”

**Notice CPD 13-07**

Grantees must maintain adequate records and documentation in support of all costs, as set forth in 24 CFR 570.502 and 570.506, and Part 85.20, standards for financial management systems. Additionally, the grantee’s records should clearly show there is a consistent treatment of like costs under similar circumstances.

**Notice CPD 13-07**

Housing rehabilitation administration is the only activity that has a separate IDIS matrix code that allows for the allocation of administrative costs as ADCs [activity delivery costs]. This category is used to charge housing rehabilitation administration costs for all CDBG-assisted housing rehabilitation and housing rehabilitation carried out using other funding sources that meet all CDBG program requirements. For other program-type activities, general program administrative costs are treated as PACs [program administrative costs] and subject to the 20 percent cap. For this reason, grantees operating programs must use care in identifying which costs can be consistently treated as ADCs (i.e., part of delivering a final cost objective) versus those costs that are identified as general administration costs.

**Notice CPD 13-07**

It is important to recognize that staff time allocable as ADCs represents the actual time spent on implementing and completing an eligible CDBG activity.

**Guide to National Objectives and Eligible Activities for Entitlement Communities (Chapter 2)**

*Complying with National Objectives - Rehabilitation:* Section 105(c)(3) of the authorizing statute, the Housing and Community Development Act of 1974, requires that, in order for an activity that involves the acquisition or improvement of property for housing to qualify as benefiting L/M [low and moderate] income persons, the housing must be occupied by such persons. Even though a particular housing activity may provide a clear benefit to an area containing predominantly L/M Income residents, it cannot qualify on that basis. Instead, the housing must be occupied by L/M Income households.

**Guide to National Objectives and Eligible Activities for Entitlement Communities (Chapter 2)**

*Eligible Types of Properties –* CDBG funds may be used to finance costs of rehabilitation of nonprofit-owned, nonresidential buildings and improvements that are not considered to be public facilities or improvements under §570.201(c) of the CDBG program regulations.

**Guide to National Objectives and Eligible Activities for Entitlement Communities (Chapter 2)**

*Eligible Activities*- The regulations specify that facilities that are designed for use in providing shelter for persons having special needs are considered to be public facilities (and not permanent housing), and thus are covered under this category of basic eligibility. Such shelters would include transitional facilities/housing for the homeless

**Guide to National Objectives and Eligible Activities for Entitlement Communities (Chapter 2)**

*Drawing Down Funds for Rehabilitation* - The general Treasury rules for drawing Federal funds require that funds not be drawn until needed. In the CDBG program, this usually means that the grantee or subrecipient should not draw funds from the line of credit (the Treasury) in an amount greater than that which it expects to use within the next three business days.

**Modesto Homeowner Rehabilitation Program Polices 4.7.5**

Housing Rehabilitation Specialist processes approved projects through the bid process.

**Modesto Homeowner Rehabilitation Program Polices 10.2**

A minimum of three bids by California Licensed Contractors shall be obtained prior to bid approval consideration.

**Modesto Homeowner Rehabilitation Program Polices 17.7**

Contractor progress payments shall be subject to Housing Rehabilitation Specialist verification, acknowledgement and certification that the work being invoiced for is reflective of the work verified through the Housing Rehabilitation Specialist's progress inspection(s) and through the time period indicated on the payment request.

**Modesto Homeowner Rehabilitation Program Polices 17.8**

Contractor payment requests will only be processed if signed by the Contractor, Homeowner, Housing Rehabilitation Specialist, and Housing Rehabilitation Specialist Supervisor. Invoices must be detailed enough to determine payment eligibility, along with accompanying documentation. All efforts will be made to reimburse qualified invoices within a 30-day time frame.

**Modesto Purchasing Manual**

A bidder's conference will be scheduled eight (8) days after the bid issue date. The department shall receive an email appointment. Vendors shall have the opportunity to ask questions for clarification of bid specifications.