



**City of Newark, New Jersey
Generally Obligated and Expended NSP1 Funds
in Accordance With Regulations, but Had
Weaknesses in Administrative Controls**



Issue Date: July 20, 2012

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TO: Annemarie Uebbing, Director, Office of Community Planning and Development,
Newark, NJ, Field Office, 2FD

Edgar Moore

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

SUBJECT: The City of Newark, NJ, Generally Obligated and Expended NSP1 Funds in
Accordance With Regulations, but Had Weaknesses in Administrative Controls

Enclosed 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 Newark, NJ's administration of its Neighborhood Stabilization Program (NSP1), funded under Title III of Division B of the Housing and Economic Recovery Act of 2008.

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 8L, requires that OIG post its publicly available reports on the OIG Web site. 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.



July 20, 2012

The City of Newark, NJ, Generally Obligated and Expended NSP1 Funds in Accordance With Regulations, but Had Weaknesses in Administrative Controls

Highlights

Audit Report 2012-NY-1009

What We Audited and Why

We audited the City of Newark, NJ's administration of its Neighborhood Stabilization Program (NSP1), funded under Title III of Division B of the Housing and Economic Recovery Act of 2008, in support of the Office of Inspector General's (OIG) goal to improve the U.S. Department of Housing and Urban Development's (HUD) execution of and accountability for its fiscal responsibilities. We selected the City based upon a risk assessment that considered that the City was awarded the second highest amount of funds among the Newark field office's six grantees and received the highest HUD risk assessment score (70). The objective of the audit was to determine whether the City officials properly obligated and expended NSP1 funds.

What We Recommend

We recommend that HUD instruct City officials to (1) reimburse the City's line of credit for the \$11,250 paid and deobligate the additional \$11,250 budgeted for ineligible consultant fees, (2) provide support for the \$49,275 unsupported consultant fees paid, (3) report and use the \$111,943 in program income not realized before drawing down additional NSP1 funds, and (4) provide supporting documentation for the appraisal of an NSP1-developed property.

What We Found

City officials generally obligated NSP1 funds in a timely manner for eligible activities and expended funds in accordance with HUD regulations. However, there were weaknesses in administrative controls. Specifically, City officials approved ineligible and unsupported consultant fees, did not properly report program income, and did not always properly maintain program records. Consequently, \$60,525 expended and \$11,250 obligated for consultant fees was not available for eligible costs, program income of \$111,943 was not available for use, and HUD was not adequately informed of program income generated. In addition, some of the NSP1-funded activities had experienced delays that would require city council approval for extensions.

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BACKGROUND AND OBJECTIVES

The Neighborhood Stabilization Program (NSP1) was authorized under Division B, Title III, of the Housing and Economic Recovery Act of 2008 and provided \$3.92 billion to stabilize communities through the purchase and redevelopment of foreclosed-upon and abandoned residential properties. HUD's Community and Economic Development Program division administered the funds as Community Development Block Grants. Grants were awarded to all States, Puerto Rico, and selected local governments on a formula basis to address the greatest need as determined by the U.S. Department of Housing and Urban Development (HUD). Grantees were required to obligate all of their funds within 18 months and expend the funds within 4 years, from the date HUD signed their grant agreements.

NSP1 funds could be used to buy, rehabilitate, and resell or rent foreclosed-upon and abandoned homes. Grantees could develop their own programs and funding priorities, but at least 25 percent of the funds were required to be used for the purchase and redevelopment of abandoned and foreclosed-upon homes or residential properties that would be used to house individuals or families whose incomes did not exceed 50 percent of the area median income. Any program income realized was to have been expended before additional drawdowns of NSP1 grant funds were requested from HUD. Grantees could use up to 10 percent of their funds, including any program income, for administrative and planning costs.

HUD awarded the City of Newark approximately \$3.4 million in NSP1 grant funds on March 18, 2009. The City obligated its funds for administrative costs and awards to six subgrantees for the purchase and rehabilitation of 36 abandoned or foreclosed-upon homes. As of March 2012, City officials had expended \$1.7 million, or 50 percent, of the \$3.4 million in NSP1 funds awarded.

The City was awarded the second highest amount among the Newark field office's six grantees and received the highest HUD risk assessment score (70). In addition, HUD's monitoring found that the City's subrecipients' ability to acquire abandoned and foreclosed-upon properties in the identified areas of greatest need was an impediment to program accomplishment.

The audit objective was to determine whether City officials properly obligated and expended the City's NSP1 funds for stabilization and redevelopment activities.

RESULTS OF AUDIT

Finding 1: City Officials Generally Obligated and Expended NSP1 Funds in Accordance With Regulations but Had Weaknesses in Administrative Controls

City officials generally obligated NSP1 funds in a timely manner for eligible activities and expended funds in accordance with HUD regulations. However, there were weaknesses in the City’s administrative controls. Specifically, City officials approved ineligible and unsupported consultant fees, did not properly report program income, and did not always properly maintain program records. These conditions occurred due to weaknesses in administrative controls and officials’ unfamiliarity with HUD regulations. Consequently, \$60,525 of unsupported and ineligible consultant fees, and an additional \$11,250 obligated, was not available for eligible costs, program income of \$111,943 was not available for use, and HUD was not adequately informed of program income generated. In addition, some of the NSP1-funded activities had experienced delays that would require city council approval for extensions.

Funds Were Obligated in a Timely Manner

City officials established adequate controls to ensure that all funds would be obligated within 18 months of their availability as required by section 2301(C)(1) of the Housing and Economic Recovery Act of 2008. NSP1 funds were made available to the City on March 18, 2009, and City officials obligated \$3.2 million before the September 18, 2010, deadline for the acquisition and rehabilitation or construction of 36 NSP1-eligible properties as follows:

Subgrantee	Amount	Subgrantee award date	Number of properties
Episcopal Community Development	\$ 760,000	July 1, 2009	9
La Casa De Don Pedro Development Corporation	760,000	July 1, 2009	10
Greater Newark Housing Partnership	906,165	July 1, 2009	9
Housing and Neighborhood Development Services, Inc.	400,000	July 1, 2009	4
Unified Vailsburg Services Organization, Inc.	120,000	July 1, 2009	3
Life Management, Inc.	120,000	July 1, 2010	1
Total	\$3,066,165		36

An additional \$220,000 was retained for City administrative expenses.

Funds Were Generally Expended for Eligible Costs

As of March 2012, HUD's Disaster Recovery Grant Reporting (DRGR) system reported that City officials had drawn down \$1.7 million, or 50 percent, of the \$3.4 million in NSP1 funds for costs claimed by six subgrantees or City administrative expenses. Documentation in support of the \$1.7 million drawdown disclosed that the funds had generally been disbursed for eligible activity related to the purchase and rehabilitation of 16 abandoned or foreclosed-upon homes and the sale of 4 of them. However, there were some ineligible and unsupported costs paid due to weaknesses in controls over the budgeting and disbursement of funds.

There Were Ineligible and Unsupported Costs

HUD's NSP Policy Alert, dated August 27, 2010, and updated November 16, 2011, provides that paying developer fees for a project manager is double-dipping and would not be allowed. However, although City officials paid consultant fees of \$11,250 to one subgrantee and obligated an additional \$11,250 in consulting fees, \$40,413 in developer fees was also budgeted for the same project.

A City subgrantee paid its contractor an unsupported \$49,275 in consultant fees related to the sale of an NSP1-developed property on September 30, 2010. The contract between the subgrantee and its contractor provided for a consultant fee based upon the services provided according to the redevelopment agreement, as well as an additional consultant fee. The additional consultant fee would be based upon the net sales price of the property to a buyer identified and counseled as a result of the contractor's efforts. However, documentation provided indicated that the efforts required for the additional consultant fee were executed by the City's Department of Economic and Housing Development and Tri-City Peoples Corporation, a HUD-certified housing counseling agency.

In addition, City officials reimbursed a subgrantee for 50 percent of property's acquisition costs in excess of that allowed by City policy. City policy limits the reimbursement of acquisition costs to 25 percent of a property's actual cost. Contrary to this policy, City officials paid acquisition costs of \$90,000 on October 27, 2010, for three NSP1-eligible properties, amounting to \$30,000 per property, and reimbursed an additional \$60,000 in acquisition costs for two of the properties, along with additional rehabilitation expenses, on October 20, 2011. However, we did not classify this as an ineligible expense because HUD regulations do not limit the reimbursement of acquisition costs. These conditions existed due to weaknesses in the City's administrative control over the budgeting and disbursement of funds to subrecipients.

Program Income Was Not Properly Reported or Expended

City officials did not report or expend \$111,943 in program income realized on the sale of one of its NSP1-developed properties before drawing down additional NSP1 funds from HUD and did not report the program income as required. Federal Register Notice 194, Volume 73, page 58340, dated October 6, 2008, provides that revenue received by a State, unit of general local government, or subrecipient, as defined in 24 CFR (Code of Federal Regulations) 570.500(c), that is directly generated from the use of Community Development Block Grants constitutes program income, which should be expended before grant funds are drawn down and expended. Program guidelines further provide that when income is generated by an activity that is partially assisted with Federal funds, the income must be prorated to reflect the percentage of Federal funds used. As shown below, the City should have recognized \$111,943 in program income receipts. However, the program income amounts were not reported to HUD, nor were these amounts disclosed in the Disaster Recovery Grant Reporting System.

NSP1 property	Total cost	NSP1 funds used	Percentage of cost paid with NSP1 funds	Program income realized	Prorated program income
62 Ninth St.	\$176,000	\$ 85,075	48.3	\$ 135,238	\$ 65,320
284 South 11 th St.	160,000	79,000	49.4	84,919	41,950
60 Arlington St.	220,335	75,210	34.1	13,704	4,673
Total					\$ 111,943

City officials did not recognize or report this program income in the City’s quality performance report to HUD as required. Further, City officials approved the payment and drew down NSP1 funds of \$94,225 and \$42,696 on October 1 and December 15, 2010, respectively, for its other NSP1 projects without requiring that the subgrantee use program income earned of \$111,943 before seeking NSP1 funds. This noncompliance occurred because of City officials’ unfamiliarity with program income regulations.

Maintenance of Program Records Was Inadequate

City officials did not always maintain adequate records to determine that the City purchased properties at a discount from the properties’ current market-appraised value and that program income was earned. Section 2301(d)(1) of the Housing and Economic Recovery Act of 2008 requires that any purchase of a foreclosed-upon home or residential property under NSP1 be at a discount from the current market-appraised value, and acquisitions of foreclosure property require an appraisal to determine the statutory purchase discount. Further, HUD requires

that the appraisal be performed within 2 months of the final offer. City files lacked an appraisal for 1 of the 16 properties acquired with NSP1 funds, and City officials could not provide documentation to determine whether the property was foreclosed-upon or abandoned. This condition existed because of administrative control weaknesses.

Projects Have Experienced Delays

While the City appears to have the capacity to expend its NSP-1 funds, various projects funded with the NSP-1 funds have experienced delays. City officials initially executed agreements with the City's subgrantees that provided for up to two six month extensions without requiring City Council approval. Five of the six subgrantee agreements were extended an additional six months by the City around June 2011, and subsequently extended again in December of the same year. The current extensions expire on June 30, 2012, and will require City Council approval to extend the projects again. An assessment of the projects' status prepared by City officials disclosed that 13 of the 36 projects will not be completed by June 30, 2012, and that 13 are estimated to have less than 25 percent of construction completed. If the funds for these projects are not expended by March 18, 2013, the funds will be recaptured by HUD in compliance with the Housing and Economic Recovery Act of 2008.

Conclusion

City officials generally obligated the City's \$3.4 million in NSP1 funds in a timely manner for eligible activities and expended \$1.7 million in accordance with HUD regulations. However, there were weaknesses in administrative controls, which caused ineligible and unsupported expenditures. Thus, City officials' unfamiliarity with HUD regulations resulted in improper recognition and use of program income. In addition, some projects had experienced delays requiring that actions be taken to ensure that funds would be expended in a timely manner with proper approval.

Recommendations

We recommend that the Director of HUD's Newark, NJ Office of Community Planning and Development instruct City officials to

- 1A. Reimburse its line of credit for the \$11,250 in ineligible consultant fees paid and deobligate the additional consultant fees of \$11,250 obligated, thus ensuring that these funds can be put to better use for eligible items.

- 1B. Provide justification for the unsupported \$49,275 in consultant fees paid and if adequate support cannot be obtained, recover the costs from the subgrantee.
- 1C. Strengthen its controls over the obligation and expenditure of subgrantee costs to ensure that ineligible and unsupported consultant fees are no longer budgeted and paid.
- 1D. Record the unreported program income of \$111,943 in the Disaster Recovery Grant Reporting System so that these funds can be used before requesting additional NSP1 fund drawdowns, thus ensuring that these funds are put to better use.
- 1E. Strengthen controls over the recognition and reporting of program income to ensure that it is properly reported in HUD's Disaster Recovery Grant Reporting System and used as required before drawing down available NSP1 funds.
- 1F. Provide appraisals or other documentation for one property lacking an appraisal to determine whether the properties were purchased at a discount from the appraised value. If program income should have been recognized, it should be reported and used before additional NSP1 funds are drawn down to ensure that funds are put to better use.
- 1G. Seek city council approval for extensions of subgrantee agreements if warranted and establish controls to ensure that projects will be completed in a timely manner to ensure the expenditure of NSP1 funds before the expenditure deadline to prevent recapture.

SCOPE AND METHODOLOGY

We performed the audit fieldwork from December 2011 through April 2012 at the City's offices at 920 Broad Street, Newark, NJ. The audit covered the period March 2009 to February 2012.

To accomplish the audit objectives, we performed the following steps:

- Reviewed HUD regulations and program guidance to gain an understanding of NSP1.
- Reviewed the NSP1 agreements between HUD and the City and the agreements between the City and its subgrantees to obtain an understanding of the size and nature of the City's program.
- Documented the City's internal controls over the administration of its NSP1 to assess program risks.
- Reviewed City obligations to ensure that all funds were obligated within 18 months of receipt as required.
- Reviewed 28 vouchers through which City officials disbursed \$1.7 million in NSP1 funds and tested the disbursements to ensure that the costs complied with program regulations and were for eligible expenses, such as sales costs, closing costs, and reasonable developer fees.
- Conducted site observations of the 36 properties being rehabilitated or constructed by the City to identify any discrepancies between the rehabilitation or construction status and that reported by City officials.
- Verified the property addresses obtained from the most recent quarterly performance reports in Lexis-Nexis and the New Jersey Association of County Tax Boards Web site to determine the acquisition costs and current ownership.
- Reviewed City records to identify any program income and ensure that it was properly reported. Assessment of the reliability of the data in the City's systems was limited to the data sampled, which were reconciled to the City's records.
- Reviewed City records to ensure that home buyers were qualified and received home buyer counseling as required.

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(s).

INTERNAL CONTROLS

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

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

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

Relevant Internal Controls

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

- Program operations - Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Compliance with laws and regulations - Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding resources - Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.
- Validity and reliability of data - Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

We assessed the relevant controls identified above.

A 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:

- City officials did not ensure that program income was properly identified, recorded, and expended (see finding).
- City officials did not safeguard resources when they disbursed funds for ineligible and unsupported fees (see finding).
- City officials did not ensure the validity and reliability of data when they did not maintain adequate program records (see finding).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1A	\$11,250		\$11,250
1B		\$49,275	
1D			\$111,943
Total	<u>\$11,250</u>	<u>\$49,275</u>	<u>\$123,193</u>



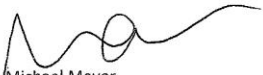
- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.
- 2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.
- 3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, if HUD implements our recommendations to require the City to deobligate the \$11,250 and to recognize program income of \$111,943, these funds would increase the NSP1 funds available, thus ensuring that the funds would be put to better use.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

<p> CITY OF NEWARK Cory A. Booker Mayor Stefan Pryor Deputy Mayor/ Director Michael Meyer Director of Housing and Real Estate Department of Economic & Housing Development Division of Housing and Real Estate</p> <p></p> <p>June 28, 2012</p> <p>Edgar Moore Regional Inspector General for Audit Office of Inspector General U.S. Department of Housing and Urban Development 26 Federal Plaza, Room 3430 New York, NY 10278 0068</p> <p>Re: City of Newark NSP-1 response to the Results of draft audit report (2012-NY-0000)</p> <p>Dear Mr. Moore:</p> <p>On June 18th, the City of Newark received a draft audit report from the U.S. Department of Housing and Urban Development's (HUD) Office of Inspector General's (OIG) for discussion purposes. This Audit Report was developed during a recent audit of the City of Newark, New Jersey Neighborhood Stabilization Program (NSP-1) funded activities.</p> <p>Attached is the City's response.</p> <p>Thank you.</p> <p>Sincerely</p> <p> Michael Meyer</p> <p>920 Broad Street • Room 421 • Newark • New Jersey 07102 • Telephone 973-733-3914 • Fax 973-733-8064 • www.ci.newark.nj.us</p>

Ref to OIG Evaluation

Auditee Comments

Comment 1

Recommendation #1A: Reimburse its line of credit for the \$11,250 in ineligible consultant fees paid and deobligate the additional consultant fees of \$11,250 obligated, thus ensuring that these funds can be put to better use for eligible items.

City of Newark Response

The draft audit report states that “paying developer fees for a project manager is double dipping and would not be allowed.” However, the expenses cited by the draft audit report are separate fees earned by separate entities for work performed and therefore do not represent “double dipping” but are usual and customary expenses with this type of transaction.

HUD’s NSP Policy Alert “Guidance on Developers, Subrecipients, and Contractors”, dated August 27, 2010 and updated on November 16, 2011 says, “...subrecipients can engage developers. However, to be treated as a developer, the entity must demonstrate ownership or control of the property to be rehabilitated or redeveloped.”

Greater Newark Housing Partnership (“GNHP” or “Sponsor”), the City’s NSP Subrecipient entered into a Site Development Agreement (“SDA”), which is attached, with Renaissance Community Development Corporation (“RCDC” or “Builder”) which obligates RCDC to, “...acquire title to the Site from the City and complete the Work described in the RDA and NSP Sub-Grant Agreements...” The SDA also sets forth that, “The Builder will endeavor to obtain a Loan from Lender to partially finance construction of the Improvements. To induce Lender to make the Loan and to secure Builder’s obligations under the Loan Documents, Builder shall subject its fee estate in the Site and the Improvements to a first lien in favor of Lender.” A Builder’s Fee, “...shall be payable only if and to the extent available from the proceeds from the sale of a home...” and will not be paid until all associated loans are repaid and outstanding sponsor and Builder expenditures are fully reimbursed. Therefore, in accordance with the above referenced Policy Alert, RCDC is assuming a majority of risk of the project, thereby enabling them to charge a developer’s fee. The \$40,413 Developer’s Fee listed on the AIA forms for the two properties is an allowable NSP expenditure, which if proceeds are available at the time the property is sold, can be paid from subrecipient’s NSP funds.

GNHP is the City’s NSP subrecipient and is separate from and unrelated to RCDC. As the services performed by GNHP reflect costs incurred for performance of work related to this project, it is entitled to compensation. These services include:

- a. Track and report to the City with respect to the Builder’s compliance with minority and women owned business requirements and to facilitate coordination between the Builder’s and Newark Works and other appropriate resources for local minority and women owned businesses;
- b. Track and report to the City with respect to the Builder’s compliance with local resident hiring requirements by checking the Builder’s compliance certifications and upon request of the City, by investigating instances of noncompliance;

Ref to OIG Evaluation

Auditee Comments

- c. Track and report to the City the Builder's efforts to recruit, train and employ local residents for construction related employment opportunities and the Builder's efforts to employ ex-offenders and to assist in the coordination with Newark Works and other resources for employment placement;
- d. Track and report to the City the Builder's adherence to approved construction and development timelines and schedules and to assist in identifying strategies and recommendations to ensure compliance with approved schedules; and
- e. Facilitate project tax abatement (if available).

Therefore, no double-dipping occurred and all property related consultant and developer fees are allowable NSP expenses.

Recommendation #1B: Provide justification for the unsupported \$49,275 in consultant fees paid and if adequate support cannot be obtained, recover the costs from the subgrantee.

City of Newark Response

The \$49,275 charges identified in the draft audit report is not consultant fees. Rather, it reflects additional home improvement features beyond the original construction scope of work. Attached is the contract between Ms. Lakina Ports, homebuyer of 62 Ninth Avenue, and Jarid Jamar Construction Company for the additional work. Ms. Ports agreed to pay Jarid Jamar Construction for all costs associated with this agreed additional work. She elected to include these costs into her mortgage amount and they were thereafter reflected on the HUD-1 Settlement Statement. Attached is a copy of the communication with the HUD OIG auditors dated April 19, 2012 explaining that these fees were not for consultant work. NSP-1 funds were not used to reimburse these costs.

Recommendation #1C: Strengthen its controls over the obligation and expenditure of subgrantee costs to ensure that ineligible and unsupported consultant fees are no longer budgeted and paid.

City of Newark Response:

As stated within the City's response to HUD OIG's Recommendations #1A and #1B, the City's NSP1 program has not paid ineligible or unsupported consultant fees. The City's NSP team, which consists of a full-time Project Manager, Contract Manager, Construction Monitor, Project Assistants as well as members of the Accounting and Finance Departments are consistently monitoring and reviewing subgrantee expenditures to ensure that the program remains in good standing and is in compliance with all federal rules and regulations. Further, the City regularly meets with and consults the HUD designated NSP Technical Assistance provider to review regulatory eligibility issues and ensure that program rules are followed.

Comment 2

Comment 3

Ref to OIG Evaluation

Auditee Comments

Comment 4

Comment 5

Recommendation #1D: Record the unreported program income of \$111,943 in the Disaster Recovery Grant Reporting System so that these funds can be used before requesting additional NSP1 fund drawdowns, thus ensuring that these funds are put to better use.

City of Newark Response:

The City has required subrecipients to price all home sales to the lesser of the appraised value or the total development costs minus NSP subsidy, in order to avoid the realization of program income. The draft audit report inaccurately reflected Total Development Costs and Net Sales Prices, and therefore, program income generated. Listed below are the final total development costs and final net sales price amounts for the below listed properties. As you will note, each property was sold for less than the property's total development cost. For 62 9th Avenue and 284 S. 11th Street, no gross income was generated from the sale of properties acquired and/or improved with NSP, thus, no program income was realized. For 60 Arlington Avenue, total development costs at the time the project was completed were less than anticipated. Therefore the project did generate prorated program income in the amount of \$2,034.37; this amount remained with the subrecipient; DRGR will be updated to reflect this information.

Attached are the itemized total development costs for each property.

NSP1 Property	Total Development Costs	Property Net Sales Price	NSP Funding	Percentage of costs paid with NSP1 funds	Program Income realized	Prorated program income
62 Ninth Avenue	\$279,275	\$199,275	\$80,000			
284 South 11 th Street	\$235,200	\$155,200	\$80,000			
60 Arlington Avenue	\$282,674.92	\$215,000	\$75,210	27%	\$7,535.08	\$2,034.37

Recommendation #1E: Strengthen controls over the recognition and reporting of program income to ensure that it is properly reported in HUD's Disaster Recovery Grant Reporting System and used as required before drawing down available NSP1 funds.

City of Newark Response:

The City has required subrecipients to price all home sales to the lesser of the appraised value or the total development costs minus NSP subsidy, in order to avoid the realization of Program Income. Each property assisted with NSP-1 funds is being reviewed to ensure no program income is generated.

Comment 6

Ref to OIG Evaluation

Auditee Comments

Comment 7

Recommendation #1F: Provide appraisals or other documentation for the two properties lacking an appraisal to determine whether the properties were purchased at a discount from the appraised value. If program income should have been recognized, it should be reported and used before additional NSP1 funds are drawn down to ensure that funds are put to better use.

City of Newark Response:

933 South 19th Street

NSP requires an appraisal for foreclosed properties if the anticipated value is greater than \$25,000. Attached is an e-mail, which was sent to _____ on April 19, 2010, which informed him that no appraisal was conducted for 933 South 19th Street, since the sales price was less than the \$25,000 threshold amount. Attached is contract of sale, showing the purchase price for this property was \$16,798.00.

Comment 8

256 S. Eleventh Street

An appraisal ("BPO") was conducted, which is attached. As you will further note, the BPO expresses that comparable sales and listed properties in the area, are at least \$15,000 to \$30,000 above the acquisition price of 256 South 11th Street.

Comment 9

Recommendation # 1G

As per the City's explanation at their Exit Conference with the HUD OIG on Tuesday, June 27th, the OIG auditors decided to withdraw this Recommendation.

Recommendation #1H: Seek City Council approval for extensions of subgrantee agreements if warranted and establish controls to ensure that projects will be completed in a timely manner to ensure the expenditure of NSP1 funds before the expenditure deadline to prevent recapture.

City of Newark Response:

Comment 10

All contractual agreements are approved by the City's Municipal Council. The City decided prior to executing the NSP agreements, to include two-6 month extensions provisions, since the extended termination date would be prior to the City's statutory deadline this would still give the City time to seek additional Council approvals and/or make changes to ensure all NSP funds are expended in a timely manner to prevent any recapture. The NSP1 statutory 100% expenditure deadline is March 18, 2013.

Additionally, the City's NSP team meets regularly with subrecipients, collect regular progress and financial reports, have various site inspection and field audits, has contracted with and relied on several TAs providers (for both City support and sub recipient support). As you are aware, we reprogrammed funds from one sub recipient due to inadequate early progress in utilizing funds as well as assisted with acquisitions through the City inventory of foreclosed and abandoned properties and advocacy and support of NCST.

Ref to OIG Evaluation

Auditee Comments

Comment 10

Although, construction of the all properties within the City's NSP1 portfolio may not be completed by March 18' 2013, the City are confident with the current team and established controls the entire NSP1 allocation will be expended.

OIG Evaluation of Auditee Comments

- Comment 1** We concur with City officials that the subrecipient's contractor meets the definition of a developer and in accordance with HUD's NSP Policy Alert would be entitled to a developer fee. However, while City officials note that the consultant and developer fees are separate fees earned by both the subrecipient and the contractor, the documentation provided (AIA document G702) shows that both the consultant and developer fees were paid to the contractor. Therefore, unless City officials can document that both fees were not earned by the contractor, we maintain that the \$11,250 paid and the additional \$11,250 as consultant fees should be classified as an ineligible cost. These costs will be resolved during the audit resolution process with HUD.
- Comment 2** City officials state that the questioned \$49,275 cost is not a consultant fee, but rather, home improvement expenses outside the contracted scope of work which the homebuyer agreed to pay. To support this position, City officials provided a contract between the home buyer and the contractor specifying work to be done for not more than \$50,000. However, the HUD-1 documenting the sale of the NSP-developed property reports the \$49,275 as being paid from the seller's proceeds of sale, and no documentation was provided to show these costs were paid from funds of the buyer. Further, the contract between the subrecipient and its contractor provided for a consultant fee of \$49,275 for identifying a buyer, providing counseling, and assisting with the closing of the NSP-developed property. Documentation indicates that this fee was calculated by deducting \$150,000 from the net sales price of \$199,275 as stipulated in the contract. However, since documentation obtained during the audit disclosed that these services were performed by another entity, we maintain that the City should provide justification for the unsupported \$49,275 in consultant fees paid to the contractor. These costs will be resolved during the audit resolution process with HUD.
- Comment 3.** We agree with the actions that City officials note they perform, but the need to strengthen procedures will depend upon HUD's resolution of the questioned costs identified in recommendation 1A and 1B.
- Comment 4** City officials state that the draft report inaccurately reflected total development costs and net sales prices, and therefore, the program income generated. They further stated that they require subrecipients to price home sales to the lesser of the appraised value or the total development costs minus the NSP subsidy in order to avoid the realization of program income, and that each property questioned was sold for less than its development cost. While City officials report additional developmental cost amounts not provided during the audit for the 62 Ninth Avenue and 284 South 11th Street properties, they did not provide documentation to support the additional costs that were part of the professional fees and financing/related charges categories. City officials will need to provide

documentation to support these additional costs as part of the audit resolution process with HUD.

- Comment 5** City officials acknowledge that the 60 Arlington Avenue property realized program income, and have agreed to update the DRGR to reflect the income; however, they calculate a lower amount due to additional claimed development costs that were not provided during the audit. However, since they did not provide documentation to support these additional costs, they will need to provide the documentation as part of the audit resolution process with HUD.
- Comment 6** City officials' comment is responsive to the recommendation.
- Comment 7** City officials maintain that an appraisal was not required for the 933 South 19th Street property because the sales price was \$16,798, which is below the \$25,000 threshold requiring an appraisal. However, while the purchase and sale agreement lists the total adjusted sales price as \$16,798, the purchase price is listed as \$29,700 and the HUD-1 reports the purchase and sale price as \$29,700. While City officials maintain that anticipated value can be interpreted as the actual purchase of the property or the actual monetary amount that was given to the seller, we believe that the anticipated value of the property should be viewed as the value that was extended by the seller, in this case \$29,700, despite the actual. Thus, City officials' interpretation of anticipated value may lead to the circumvention of the appraisal requirement of the NSP1 guidelines. Therefore, the OIG maintains its position that an appraisal, or suitable substitute for an appraisal was needed for the property acquired at 933 South 19th Street.
- Comment 8** City officials maintain that a Broker's Price Opinion meets the NSP1 requirement for an appraisal because it considers comparable sales and listed properties in the area. OIG concurs with City officials that the Broker's Price Opinion is a suitable substitute for an appraisal, and has adjusted the report to reflect such.
- Comment 9** Based upon discussion at the exit conference, the OIG agreed that HUD NSP1 guidance permits a grantee to determine what constitutes a substantial change that would require an amendment to a grantee's action plan. Consequently, since City officials had not deemed the change in assisted properties as substantial, and had advised that the DRGR system was updated, we removed the recommendation relating to strengthening controls to ensure action plans are amended when required.
- Comment 10** As acknowledged by City officials, and disclosed in the report, the initial subgrantee agreements approved by the City's municipal council included two 6-month extension provisions. However, as noted in the report, both of these extensions were executed and have since expired, and no additional extensions have been sought or approved by the council as required. While City officials maintain that they are actively monitoring the subgrantees and are confident that existing controls will ensure that the City will meet the disbursement deadline;

since 13 of 36 projects have not yet been completed, we believe it is necessary that council approval be sought to extend the subgrantee agreements. In addition, controls should be established to ensure that the remaining NSP1 funds are appropriately expended within the statutory deadline of March 18, 2013.