

**GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE INSPECTOR GENERAL**

**AUDIT OF THE DEPARTMENT OF HOUSING AND
COMMUNITY DEVELOPMENT'S MANAGEMENT
OF FUNDS PROVIDED TO COMMUNITY
DEVELOPMENT CORPORATIONS**



**CHARLES C. MADDOX, ESQ.
Inspector General**

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Inspector General

Charles C. Maddox, Esq.
Inspector General



February 22, 2000

Othello Mahone, Interim Director
Department of Housing and Community Development
801 North Capitol St., N.E.
Washington, D.C. 20002

Dear Mr. Mahone:

Enclosed is the report summarizing the results of our audit of the Department of Housing and Community Development's (DHCD) administration of funds it provided to the Community Development Corporations (OIG-11-99CD).

Specifically, our audit revealed that DHCD needed to:

- Manage its funds more effectively and establish a performance measurement system;
- Effectively monitor projects and account for the funds used for administratively funded projects;
- Account for \$11,745,000 in expenditures for two projects;
- Ensure controls are improved over conflict of interest at Community Development Corporations;
- Improve records management and locate missing records for Community Development Block Grant efforts, totaling \$7,321,282; and
- Improve its internal auditing function to comply with government auditing standards and allocate audit resources to areas with higher risk to fraud, waste, and mismanagement.

In order to facilitate the audit effort, we provided a Management Alert Report to DHCD on improving the financial disclosure process and resolving conflicts of interest (Exhibit 1). DHCD indicated, prior to a draft of this report, that it had completed actions to improve the financial disclosure process; its actions should improve the process for detecting and resolving actual and apparent conflicts of interest for its employees (Exhibit 2). We also issued a Management Alert Report (Exhibit 3) concerning the accuracy of testimony provided to Councilmembers and the adequacy of written procedures and controls for responding timely to Councilmembers' questions.

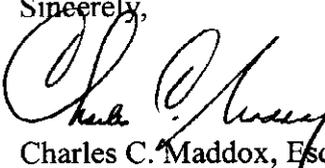
DHCD's responses (Exhibit 9) to a draft of this report are generally responsive to the intent of the recommendations. However, DHCD's responses did not include a target date to complete planned action for recommendation 7.d. and needs more time to respond to recommendations

8.a. through 8.e. regarding the internal auditing function at DHCD. In addition, recommendation 4 remains unresolved. DHCD should reconsider its position on recommendation 4 and provide documents that substantiate actual disbursements, totaling \$11,500,000, and time sheets and other documentation we requested that support the propriety of \$245,000 paid to a contractor.

Generally, audit recommendations should be resolved within 6 months of the date of the final report. Accordingly, we will continue to work with DHCD to reach final agreement on recommendation 4. DHCD, by March 22, 2000, should readdress recommendation 4, provide a target date for recommendation 7.d., and provide responses for recommendations 8.a. through 8.e. DHCD should also keep us informed when planned action dates are met or need to be extended so that the information may be entered into our recommendation tracking system.

If you have questions about this audit report, please call me or John N. Balakos, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,



Charles C. Maddox, Esq.
Inspector General

Enclosure

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TABLE OF CONTENTS

	Page
EXECUTIVE DIGEST.....	i
OVERVIEW	ii
CONCLUSIONS	ii
CORRECTIVE ACTIONS	ii
INTRODUCTION.....	1
BACKGROUND	2
OBJECTIVES	4
SCOPE AND METHODOLOGY.....	4
OTHER ISSUES.....	5
FINDINGS AND RECOMMENDATIONS.....	6
FINDING 1: MEASURING DHCD’S EFFECTIVENESS AND EFFICIENCY.....	7
FINDING 2: MONITORING PROJECT PERFORMANCE.....	12
FINDING 3: ACCOUNTABILITY FOR ADMINISTRATIVELY FUNDED PROJECTS.....	19
FINDING 4: EXPENDITURES FOR CDBG ACTIVITIES	23
FINDING 5: FINANCIAL DISCLOSURE OF EMPLOYEES.....	25
FINDING 6: CONTROLS OVER CONFLICT OF INTEREST AT COMMUNITY DEVELOPMENT CORPORATIONS.....	29
FINDING 7: RECORD MAINTENANCE AND RETENTION.....	34
FINDING 8: INTERNAL AUDITING.....	39
FINDING 9: DHCD PROCEDURES FOR RESPONDING TO QUESTIONS FROM DISTRICT COUNCILMEMBERS.....	43

TABLE OF CONTENTS

	Page
EXHIBITS	46
EXHIBIT 1: MANAGEMENT ALERT LETTER REGARDING CONFIDENTIAL STATEMENTS OF EMPLOYMENT AND FINANCIAL INTERESTS.....	47
EXHIBIT 2: RESPONSE TO MANAGEMENT ALERT LETTER ON CONFIDENTIAL STATEMENTS OF EMPLOYMENT AND FINANCIAL INTERESTS.....	49
EXHIBIT 3: MANAGEMENT ALERT REPORT REGARDING DHCD TESTIMONY BEFORE THE CITY COUNCIL'S COMMITTEE ON ECONOMIC DEVELOPMENT ON JUNE 16, 1999.....	51
EXHIBIT 4: DHCD'S INITIAL RESPONSE TO THE MANAGEMENT ALERT REPORT OF SEPTEMBER 24, 1999 (EXHIBIT 3).....	56
EXHIBIT 5: LETTER TO THE MAYOR, OCTOBER 19, 1999; RE: (EXHIBITS 3 AND 4).....	62
EXHIBIT 6: DHCD'S RESPONSE TO EXHIBIT 5.....	66
EXHIBIT 7: SCHEDULE OF COMMUNITY DEVELOPMENT PROJECTS	69
EXHIBIT 8: SCHEDULE OF ADMINISTRATIVELY FUNDED PROJECTS	70
EXHIBIT 9: DHCD RESPONSES TO THE REPORT, FINDINGS, AND RECOMMENDATIONS.....	72

**EXECUTIVE
DIGEST**

EXECUTIVE DIGEST

OVERVIEW

This report summarizes the Office of the Inspector General's audit of the Department of Housing and Community Development's (DHCD) management of funds that it provided to Community Development Corporations during the 6-year period, fiscal years 1994 through 1999. The audit was conducted at the request of a District of Columbia Councilmember, who had concerns about the appropriate use of Community Block Development Grant funds.

The U.S. Department of Housing and Urban Development provided Community Development Block Grant (CDBG) funds to DHCD, which in turn, provided funding to the Community Development Corporations (CDC).

CONCLUSIONS

This report contains nine findings that include the details supporting the conditions we observed and documented. We believe improvements by DHCD are needed to: measure its effectiveness and efficiency, monitor project performance, account for administrative funding used for projects, control expenditures for CDBG activities, detect and resolve employee conflicts of interest, detect and resolve conflicts of interest of CDC employees, retain records in accordance with regulations, improve internal auditing, and respond to questions from District Councilmembers.

CORRECTIVE ACTIONS

We directed 23 recommendations to the Director, Department of Housing and Community Development, that we believe are necessary to correct the deficiencies noted in the 9 findings included in this report. The recommendations, in part, center on:

- Establishing a strategic plan that outlines specific improvements that DHCD will commit to over the period and that incorporates a performance measurement system for projects;
- Developing, documenting, and implementing procedures and controls to ensure projects are monitored;
- Providing to the Office of the Inspector General supporting documentation for eight terminated projects and the six other specific projects that was not provided to the auditors during the course of the audit;
- Establishing procedures and controls that ensure DHCD awards its grants and subgrants with provisions requiring CDCs and other grant and subgrant recipients to track administrative costs by project;

EXECUTIVE DIGEST

- Ensuring the CDCs and other recipients of DHCD grants or subgrants awarded in FY 2000 and subsequent years, have an adequate cost tracking or allocation process in place before paying vouchers for administrative costs.
- Providing to the Office of the Inspector General the documentation to support the disbursements made for the Good Hope Marketplace Project and the New York Avenue Metrorail Feasibility Station Study;
- Improving the financial disclosure process to avoid conflicts of interest (Action is completed);
- Improving the process for detecting and resolving conflicts of interest at the CDCs so that recipients of CDBG funds have written standards of conduct that address all applicable elements of Title 24, Sections 570.611, 85.36.b.(3), and 84.42;
- Improving the procedures and controls that ensure DHCD employees adhere to record keeping and retention requirements of District regulations;
- Locating missing documents and related files identified in Table C and mark the files so that they are retained for potential future audit by the Office of the Inspector General;
- Improving DHCD's internal audit effort and ensuring that the Audit Division and its auditors are in compliance with Government Auditing Standards; and
- Providing to the OIG the approved written controls and procedures that ensure DHCD responds timely to Councilmember and Committee requests for information.

DHCD's responses to our draft report were generally adequate to correct the conditions noted. However, DHCD omitted target dates for recommendation 7.d. and requested additional time to respond to recommendations 8.a through 8.e. Recommendation 4 remains unresolved. In order to resolve recommendation 4, DHCD needs to provide the documentation we have repeatedly requested that would substantiate disbursements and transactions totaling \$11,745,000.

The full text of audit responses is included in Exhibit 9. However, DHCD responses are summarized and incorporated into each finding.

I N T R O D U C T I O N

INTRODUCTION

BACKGROUND

The Office of the Inspector General (OIG) has completed an audit of the Department of Housing and Community Development (DHCD) administration of the Community Development Block Grant (CDBG) funds provided to the Community Development Corporations (CDCs). The audit was conducted at the request of a member of the District of Columbia City Council due to concerns raised regarding the efficient use of the CDBG funds.

Mission. The mission of DHCD is to: (1) promote economic development initiatives; (2) create and maintain stable and viable mixed income neighborhoods; (3) maintain and expand the city's tax base; and (4) encourage self-sufficiency in its housing programs and policies. To aid in the fulfillment of its mission, DHCD uses the Community Development Block Grant Entitlement program (the Program), which acts as a medium through which the granting of funds takes place. The Program, which is administered by the U.S. Department of Housing and Urban Development (HUD), provides for grants of CDBG funds to housing authorities and agencies of metropolitan cities and urban counties. The determination of the grant amount is calculated by applying formulas that consider a community's population, poverty level, extent of overcrowded housing, age of housing, and growth lag. DHCD must submit certain certifications and a one-year action plan to HUD describing how the funds will be used for community development activities.

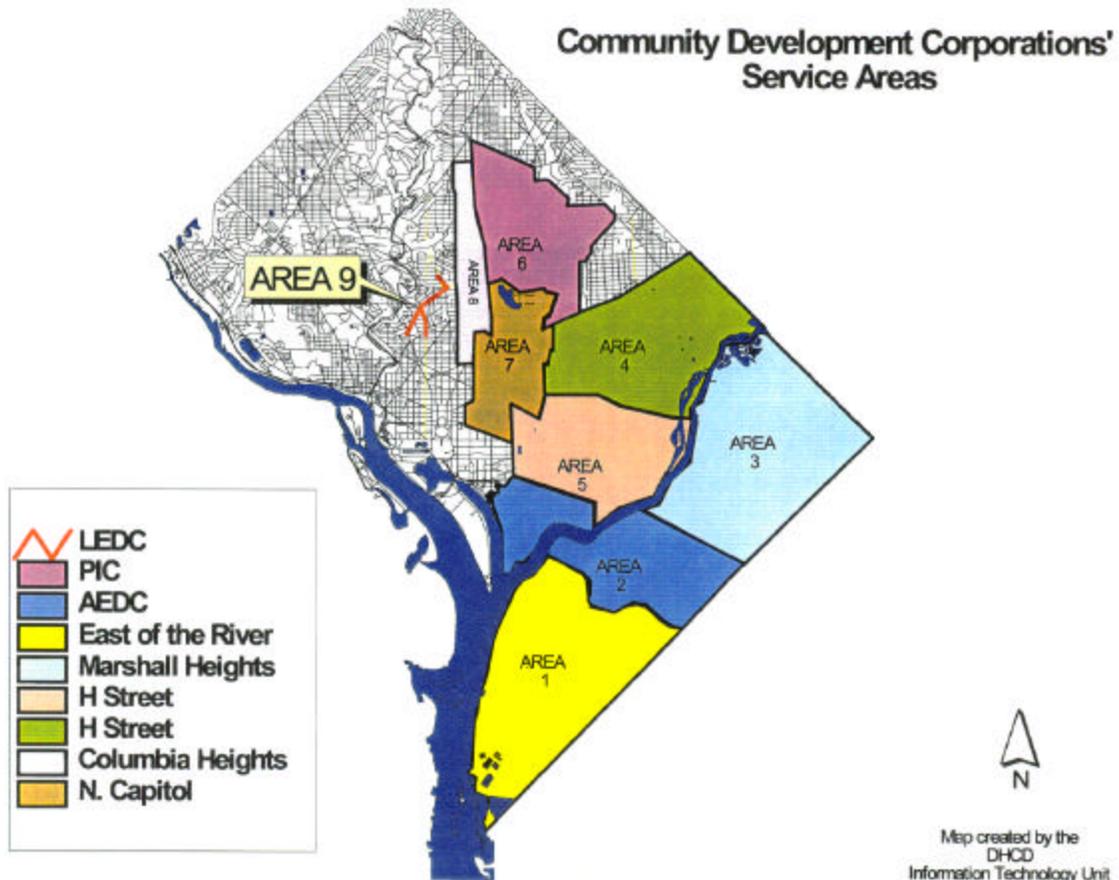
The Program. CDBG funds can be used for 25 specific activities, which for example, include: (1) acquisition of real property; (2) the acquisition, construction, reconstruction, or installation of public works, facilities and sites, or other improvements, including removal of architectural barriers that restrict accessibility of elderly or severely disabled persons; (3) clearance, demolition, and removal of buildings and improvements; (4) payments to housing owners for losses of rental income incurred in temporarily holding housing for the relocated; and (5) disposition of real property acquired under this program. Nonetheless, all activities undertaken must meet one of three national objectives of the Program. Activities must benefit low and moderate-income persons; eliminate slums or blight; or meet community development needs having a particular urgency. One way that DHCD implements the Program is by using CDCs.

Community Development and Support Initiative and the CDCs. One of DHCD's major initiatives is Community Development and Support Services. The initiative was designed to create jobs and business opportunities for District residents, as part of efforts to create and maintain healthy and viable neighborhoods. This initiative has several benefits, including the creation of a stronger tax base, stabilizing neighborhoods, and providing more income to afford increasing housing costs. An important vehicle for achieving expansion and diversification of the District's economy is to build and increase the capacity of the neighborhood CDCs to stimulate economic development activity in their respective service areas.

A CDC is a community-based non-profit organization with the capacity to complete both neighborhood development projects (commercial and residential) and neighborhood

INTRODUCTION

revitalization activities, with an emphasis on job retention and creation and technical assistance to businesses. DHCD, using subgrants and loans, provided CDBG funding to eight CDCs during most of the period under audit. The insert that follows, provided by DHCD, shows the eight CDC areas; one CDC has more than one area.



CDC Legend:

- | | |
|--|--------|
| Latino Economic Development Corporation | LEDC |
| Peoples Involvement Corporation | PIC |
| Anacostia Economic Development Corporation | AEDC |
| East of the River Community Development Corporation | ERCDC |
| Marshall Heights Community Development Corporation | MHCDC |
| H Street Community Development Corporation – Service Area #4 | HSCDC4 |
| H Street Community Development Corporation – Service Area #5 | HSCDC5 |
| Development Corporation of Columbia Heights | DCCH |
| North Capitol Neighborhood Development Corporation | NCNDC |

INTRODUCTION

OBJECTIVES

The audit objectives were to determine whether DHCD:

1. Managed and used resources in an efficient, effective, and economical manner;
2. Complied with the requirements of applicable laws, regulations, policies and procedures; and
3. Implemented internal controls to prevent or detect material errors and irregularities.

SCOPE AND METHODOLOGY

HUD provided CDBG funds to DHCD totaling \$150 million for the 6-year period, fiscal year 1994 through 1999. DHCD provided a large portion of those funds to the CDCs. The audit included a review of records and controls to support \$46.4 million that DHCD provided to the eight CDCs via subgrants and loans over the 6-year period. This amount included subgrants and loans, totaling \$27.6 million, for the CDCs to undertake 34 community development projects, and subgrants, totaling \$18.8 million, for the CDCs to provide administrative support for 74 projects and other economic development efforts. Audit objectives were applied to the areas of monitoring development activities, eligibility for program funds, maintenance of records, strategic planning, financial management, procurement, and grant administration.

We reviewed project files that included subgrants and/or loan agreements, commitment letters, and other related documents. We judgmentally selected and reviewed employee financial disclosure statements, personnel records, internal audit capability, and organization charts and functions. We also visited the CDCs and observed physical progress at, and photographed, selected project sites. We interviewed representatives of HUD; Price Waterhouse & Coopers, LLP; Mitchell Titus & Company; the D.C. City Council; DHCD, each of the eight CDCs, and local community associations. In addition, we extracted financial data from the District's Financial Management System (FMS) that provided us with a detailed transaction listing of obligations, expenditures, and disbursements of DHCD for fiscal years 1994 through 1998, and to a more limited extent for fiscal year 1999.

DHCD could not provide us with accurate, complete, and timely financial records and reports showing the amount of funds awarded to the CDCs for period audited. As a result, the audit process was substantially and significantly delayed. For nearly 8 months, DHCD had the opportunity to provide subgrant and loan agreements that the Office of the Inspector General auditors had requested. In that period, the auditors met with DHCD management many times to request the documentation. In instances when DHCD did provide requested records, the records initially were incomplete and lacked modification documents and necessary attachments. Generally, but not always, the auditors obtained the modifications and attachments after repeated meetings with management. We obtained several documents from the CDCs during our site

INTRODUCTION

visits, because DHCD could not provide the documents. We did not always obtain the information we requested.

The audit covered the period October 1, 1994, to September 30, 1999. Our audit was conducted in accordance with generally accepted government auditing standards and included such tests, as we considered necessary under the circumstances.

OTHER ISSUES

These issues represent matters not fully reviewed during the audit that are provided for the information of District officials. We made no recommendations on these matters, which came to our attention during the audit, because the scope of our audit did not focus on these areas.

Loans Forgiven. We did not perform a detailed review of DHCD's loan portfolio. However, we requested information on the total amount of loans "forgiven" by DHCD during the audit period. DHCD provided for our review a schedule that showed economic development loans forgiven during that period that totaled \$6 million. We believe the amount to be higher, however, because our review of A-133 audit reports showed loans forgiven to several CDCs, which were not included on the schedule provided to us by DHCD.

Repayments to HUD. Memorandums provided by DHCD, for our review, indicate that DHCD has not repaid at least \$8 million in disallowed costs associated with prior HUD audits.

Audits of CDCs. DHCD required the CDCs to obtain audits in accordance with HUD regulations and the Office of Management and Budget Circular A-133. However, the CDCs were frequently late in complying with the subgrant terms to provide an audit report 90 days after the CDCs fiscal year ended. The subgrant terms specified December 31st for all but one of the CDCs, which had a required delivery date of March 31st. DHCD routinely granted 90-day extensions, which some CDCs also missed. Some CDCs were hard pressed to have audit reports completed by those dates because their subsidiary organizations closed their books after the CDC. We believe the subgrant requirement for delivery by December 31st has been too stringent and resulted in extra paperwork in granting extensions. Nonetheless, delivery of the audit report by March 31st appears reasonable for most of the CDCs. DHCD may want to tailor its subgrant provisions depending upon the unique circumstances of each CDC or require delivery of the audit reports by March 31st.

CDC Contractors. DHCD could not provide our office a complete and accurate listing of contractors that the CDCs used to undertake various economic development projects and activities during the period covered by the audit. As a result, we could not perform a tax compliance review, which would have determined whether all of the contractors filed and paid District taxes in a timely manner. DHCD needs to maintain records to ensure that contractors used by the CDCs are in compliance with the District's tax laws.



F I N D I N G S

&

R E C O M M E N D A T I O N S

FINDINGS AND RECOMMENDATIONS

FINDING 1: MEASURING DHCD'S EFFECTIVENESS AND EFFICIENCY

SYNOPSIS

DHCD needs to improve its effectiveness and efficiency in managing its resources. DHCD did not efficiently or effectively administer \$150 million of CDBG funds that HUD provided on grants to the District during the 6-year period that ended with fiscal year 1999. As a result, funds were not used in a prudent manner, and DHCD maintained more than \$30 million dollars in unused CDBG funds during most of the audit period; however, DHCD reduced the unused CDBG funds to \$11.4 million in fiscal year 1999. We determined that the percentage of funds used for projects was less than 20 percent in fiscal years 1996 and 1997 and improved to 60 percent in fiscal year 1998. Development projects initiated during the period were not properly monitored; administratively funded projects were not properly accounted for, and many supporting records and documents were not properly maintained. Furthermore, DHCD had not established an adequate performance measurement system and could not measure and evaluate the progress made on the projects undertaken by the CDCs. Therefore, DHCD could not make a definitive statement regarding the actual or expected rate of return or economic benefits due to the District although \$150 million has been available to improve the community. Some of the factors that contributed to DHCD's ineffective management include: continued turnover of executive management, turnover of personnel resulting from downsizing, and the lack of a serious commitment by management to a clearly defined strategic plan. A strategic plan is necessary to correct deficiencies and create clear, visible, and measurable economic benefits for the citizens of the District.

AUDIT RESULTS

DHCD did not effectively manage \$150 million in CDBG funds during fiscal years 1994 through 1999. During that period, DHCD did not use a large percentage of available CDBG funds. Notwithstanding that funds were not used efficiently, DHCD lacked a measurement system that showed that the District and the community benefited from the millions that were used.

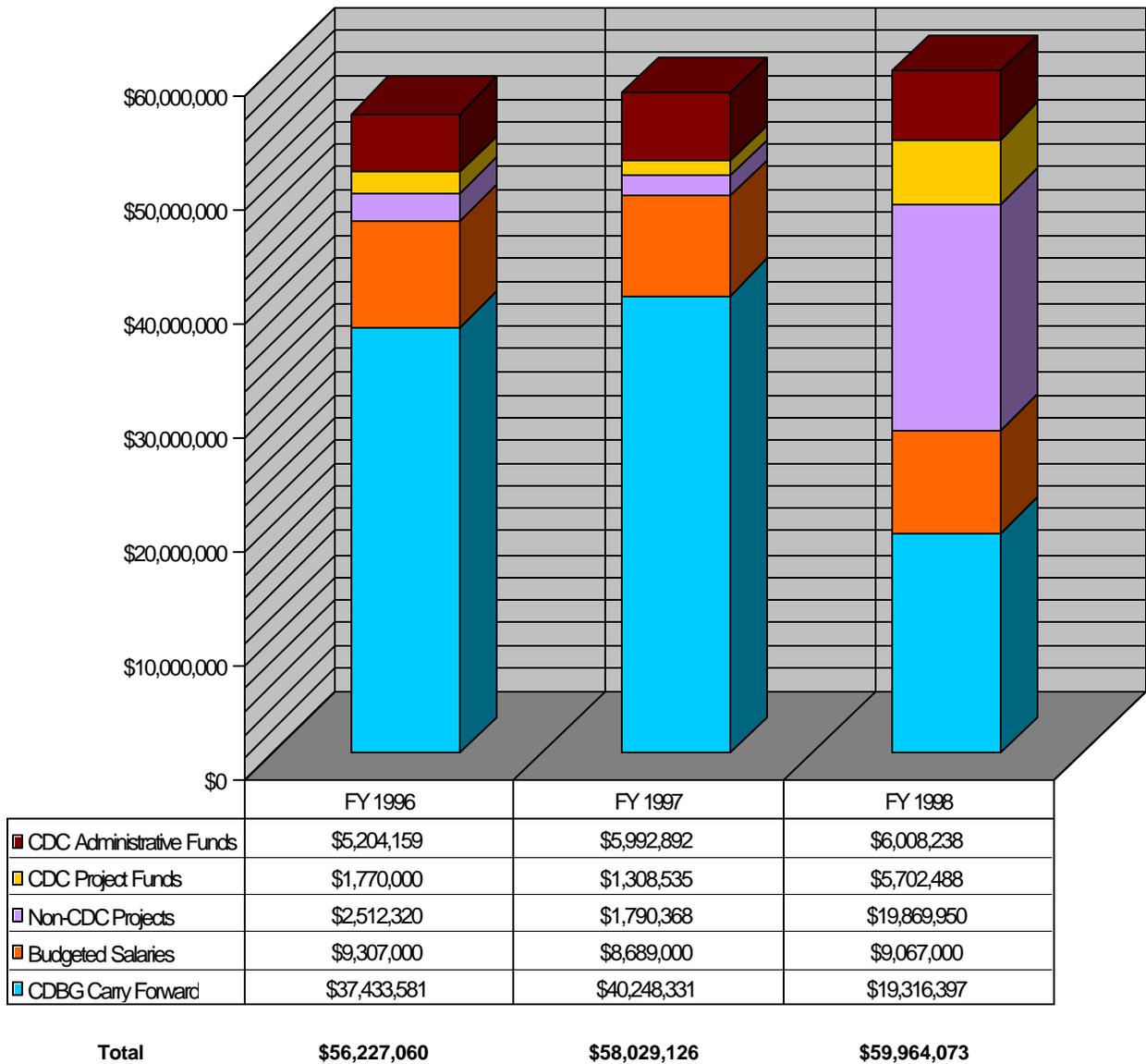
Distribution of CDBG Funds. Our analysis of the distribution of available CDBG funds showed that during fiscal years 1996 and 1997, DHCD maintained more than \$30 million of unused funds at fiscal-year end. DHCD reported that it had reduced the amount of unspent funds, referred to as the CDBG "carry forward amount," to \$11.4 million by July 1, 1999. Further analysis shows that CDBG funds distributed for projects (development and administratively funded projects) during fiscal year 1996 amounted to \$9.5 million, which was only 17 percent of available CDBG funds (\$56.2 million) for that year. For fiscal year 1997, the amount distributed for projects was \$9.1 million, 16 percent of available CDBG funds (\$58 million) for that year. The amount distributed for projects increased during fiscal year 1998 to \$43.1 million, which was 60 percent of the available CDBG funds. This increase was due to a new method of awarding subgrants for projects, referred to as the Task Force method, which was

FINDINGS AND RECOMMENDATIONS

FINDING 1: Measuring DHCD’s Effectiveness and Efficiency

used by DHCD in fiscal year 1998. The distribution of CDBG funds for fiscal years 1996 to 1998 is graphically illustrated on the Table A. We did not analyze the distribution of funds for fiscal year 1999 because year-end amounts and account balances were not finalized, as of the completion date of our fieldwork.

Distribution of CDBG Funds (FY 1996-1998)



In the insert “Distribution of CDBG Funds FY 1996 - 1998,” funds are distributed by categories; each category is defined, as follows:

FINDINGS AND RECOMMENDATIONS

FINDING 1: Measuring DHCD's Effectiveness and Efficiency

CDC Administrative Funds. This category includes all CDBG funds that DHCD obligated for administratively funded projects and other purposes and that DHCD provided to CDCs and Community Based Organizations. In most cases, DHCD issued subgrants for administrative purposes to incur these gross obligations. The amounts were traced to the Financial Management System.

CDC Project Funds. This category includes gross obligations that DHCD incurred by providing subgrants and loans to the CDCs for the actual project development and construction. The amounts were also traced to the Financial Management System.

Non-CDC Projects. Projects, and related funding, to organizations other than CDCs has been increasing. This category includes all funds obligated by subgrants and loans to subrecipients other than CDCs for projects. DHCD provided the amounts, which we did not test for accuracy.

Budgeted Salaries. Budgeted Salaries is a category we used to show how much CDBG funds that DHCD used for the salaries of its employees. DHCD provided the budgeted salary totals, which we did not compare to actual costs.

CDBG Carry Forward. This category captures the amount of CDBG funds that were not used in a year in which they were available for DHCD to obligate. The funds are then carried forward to the next fiscal year's operating budget. The amounts shown in the insert by fiscal year were the amounts available to be carried forward to the next. As such, the carry forward in one year could be included in the carry forward in the next year. The amounts of carry forward per fiscal year that we calculated are shown in the insert; however, these amounts did not agree with DHCD's figures. DHCD records showed carry forward for fiscal year 1996, 1997, and 1998 to be \$34,199,126, \$36,372,073, and \$24,794,446, respectively.

Performance Measurement System. DHCD's two divisions that managed projects had not established an adequate performance measurement system, and therefore, could not measure and evaluate the progress made on the projects undertaken by the CDCs.

The Development Finance Division funded 34 development projects through loans and subgrants of CDBG funds during the 6-year period, totaling \$27.6 million, but did not measure performance or evaluate the progress of any of the 34 projects. This division, although adequately staffed with at least 12 project managers, had not established procedures for measuring project performance and could not provide our office with any progress reviews or reports.

The Residential and Community Services Division had a system for evaluating performance but the system was inadequate. The division used a standardized program evaluation form to measure and evaluate efforts of the CDCs for administratively funded projects and other economic development activities. The form listed activities, accomplishment measures, and the specific elements for each activity or measure. Each element was rated either

FINDINGS AND RECOMMENDATIONS

FINDING 1: Measuring DHCD's Effectiveness and Efficiency

outstanding, excellent, satisfactory, satisfactory with concerns, or unsatisfactory. The activity and accomplishment measures listed on the form include: accomplishment of project tasks, outreach/marketing, technical assistance, merchant association, façade and street improvements, infrastructure improvements, timely submission of grant deliverables, and economic development activities.

The Residential and Community Services Division provided for our review all of the evaluations of the CDCs made during fiscal year 1998. None of the completed forms contained all the required quantifiable information, such as number of jobs created, loans disbursed, taxes generated, etc. We also noted that two of the CDCs were given satisfactory ratings for accomplishments related to specific administratively funded projects, for which we disagree, and in fact, question whether any progress had been made. In our opinion, the evaluations did not capture the data necessary to measure and evaluate progress, were ambiguous, and need to be improved. Using well-defined terms, baseline, target values, and target dates could better achieve clarity in performance measurement.

Conclusion. DHCD was ineffective in using CDBG funds, which resulted in a continuing carry forward of large amounts of funds from one operating budget year to the next. DHCD also lacked an effective performance measurement system that would show how funds distributed to the CDCs actually benefited the District and compared to the results anticipated. Without such a performance system, the District can not be assured that the millions available and spent were achieving a reasonable return on those millions invested. DHCD needs a comprehensive strategic plan that commits management to specific improvements in the District over a 3- to 5-year period, which is annually updated. Such a plan should help DHCD become more efficient in using available funds.

A strategic plan incorporating a performance measurement system is needed to improve management of CDBG funds. However, the plan would be of little value should executive management continue to change unless subsequent Directors and other executives “buy in” to the plan. Over the last 14 years, DHCD had at least ten Directors. During the time of our audit fieldwork, DHCD's two top executives changed.

RECOMMENDATION 1

We recommend that the Director, DHCD, establish a strategic plan that outlines specific improvements that DHCD will commit to over the period and that incorporates a performance measurement system for projects.

DHCD RESPONSE

DHCD is aware of the need to establish a strategic alignment between its projects, the District's strategic neighborhood initiatives, available funds, and its performance. A strategic plan will be developed. Target date to complete planned actions is April 30, 2000.

FINDINGS AND RECOMMENDATIONS

FINDING 1: Measuring DHCD's Effectiveness and Efficiency

OIG COMMENT

The action planned by DHCD should correct the conditions noted.

FINDINGS AND RECOMMENDATIONS

FINDING 2: MONITORING PROJECT PERFORMANCE

SYNOPSIS

DHCD issued subgrants and loans, totaling \$50.7 million, to execute at least 108 projects over the 6 fiscal years through FY 1999. The audit disclosed that DHCD did not effectively monitor the progress and status of at least 71 of those projects. We could not determine the value of 37 unmonitored projects, but the value of the remaining 34 unmonitored projects totaled \$27.6 million. DHCD officials said that project monitoring for development projects was discontinued when DHCD reorganized after reduction-in-force actions. We, however, attribute the lack of monitoring to insufficient executive and management oversight over the years. Also, DHCD allocated only 3 employees to monitor 74 projects funded by administrative subgrants. As a result, the status and progress of the projects are not readily available and projects have languished as funds have been expended. In addition, lack of monitoring precluded timely detection of delays in starting and completing projects and precluded timely detection of poor workmanship, all of which caused additional costs. Projects were also terminated without knowing the total costs incurred on those projects.

AUDIT RESULTS

DHCD issued subgrants and loans totaling \$50.7 million from the beginning of FY 1994 through FY 1999, which included \$46.4 million for 77 subgrants and loans that funded 108 projects and \$4.3 million for 11 subgrants for an undetermined number of projects. DHCD, as discussed in Finding 7, "Record Maintenance and Retention," was unable to provide the 11 administrative subgrant agreements (and other documents) for audit; therefore, the purpose and number of projects for those subgrants could not be determined.

Monitoring is the means by which DHCD can timely determine when the projects it funds are off track and need special attention to avoid wasting or otherwise misusing CDBG funds. Title 24, §85.40(a) provides for monitoring and reporting program performance. This Section provides:

Monitoring by grantees [Such as DHCD]. Grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function or activity.

DHCD had tracked the progress and status of 37 of the 74 projects funded on administrative subgrants. However, DHCD did not have similar information for the remaining 37 projects funded by administrative subgrants or for the 34 projects funded by loans and subgrants for actual project development and construction. DHCD's Development Finance Division had responsibility and authority over the subgrants and loans that funded actual project

FINDINGS AND RECOMMENDATIONS

FINDING 2: Monitoring Project Performance

development and construction, and the Residential and Community Services Division had responsibility and authority over the administratively funded subgrants. In at least nine instances, both Divisions funded a portion of a project.

Project Development and Construction Funding. The Development Finance Division funded 34 projects through loans and subgrants of CDBG funds during the 6-year period, totaling \$27.6 million. We conclude that none of the projects were effectively monitored because DHCD did not have written procedures for monitoring projects and did not prepare monitoring reports for the projects. As a result, some of the projects suffered excessive delays in starting or completing work, poor workmanship, and additional costs. Examples include the Knox Hill Village, Monterey Park, and 1429 Girard Street projects.

- The Knox Hill Village project, an initiative to build 132 townhouses, was initially funded by a series of loans beginning in September 1989 totaling \$1,150,000. These loans were in default and were consolidated in a repayment agreement. The builder has paid back only \$213,000 to date. In the meantime, DHCD provided an additional loan of \$700,000 to the builder in July 1998 to complete the project even though the builder had not repaid the original loans. As of August 1999, about 65 of the 132 townhouses had been built.
- The Monterey Park project was funded by a series of loans beginning in July 1994, totaling \$1.38 million. The project was to ultimately build 64 townhouses; however, only 8 were built from 1994-1999. Each townhouse had construction deficiencies that the Department of Consumer Regulatory Affairs found during an August 1999 inspection that listed electrical, structural, and plumbing construction deficiencies. The builder was described as financially insolvent. Homeowners have threatened to sue DHCD for failing to correct the deficiencies.
- DHCD funded the 1429 Girard Street project with subgrants and loans and is discussed in more detail under the heading “Administrative Funding,” that follows.

Administrative Funding. As discussed in Finding 3, “Accountability for Administrative Funding for Projects,” the Residential and Community Services Division did not require the CDCs to track the administrative costs for its 74 projects.

Although the Residential and Community Services Division monitored some administrative projects and prepared monitoring reports, the reports for FY 1997 and 1998 did not contain any information on 37 projects. Therefore, we could not determine the status of those projects. As a result, we requested from DHCD the status (completed, ongoing, or terminated) of the 37 projects. After 28 days, DHCD responded with a status of the projects, which disclosed that 8 projects had been terminated, 1 was suspended and then reinstated, 10 projects were ongoing, and 18 were completed. We then requested DHCD to advise us for terminated projects when and why the 8 projects were terminated and the costs incurred on those projects. DHCD did not provide information on the costs of the terminated projects or all the

FINDINGS AND RECOMMENDATIONS

FINDING 2: Monitoring Project Performance

information we requested. However, DHCD provided an explanation for the terminated projects and the year the projects were terminated. Using that information, we noted that three projects were funded beyond the termination date. The eight terminated projects, the termination dates, and periods funded after termination are shown in Table A.

Table A: Schedule of Project Terminations

<u>Project</u>	<u>Year¹ Terminated</u>	<u>Period Funded After Termination</u>
1. Terrace Manner II Townhouse	1997	None
2. New York Avenue Industrial Supply	1996	FY 1997
3. Rosedale	1998	None
4. Hayes School	1995	FY 1996 & 1997
5. MiCasa/Incubator	1997	None
6. Chaplin Woods	Unclear	None
7. Bates St./North Capitol Building	1997	None
8. Community Development Credit Union	1996	FY 1997

Site Visits. Our on-site visits to 15 projects showed that 6 projects, which DHCD had administratively funded from 2 to 5 years, did not appear to have visible physical development activity or progress. The remaining 9 projects showed visible signs of progress. DHCD provided an explanation for the lack of physical progress on the 6 projects, as follows:



1429 Girard Street, N.W. DHCD funded this project with administrative subgrants from FY 1996 through FY 1999, but the amount of administrative funds allocated to this project was unclear. In addition to the administrative funds, DHCD “awarded” the builder \$993,000 in project funds in March 1998 through a commitment letter for a loan. The project was to rehabilitate an apartment

building containing 20 units. DHCD stated to us that the vendor had scheduled a pre-

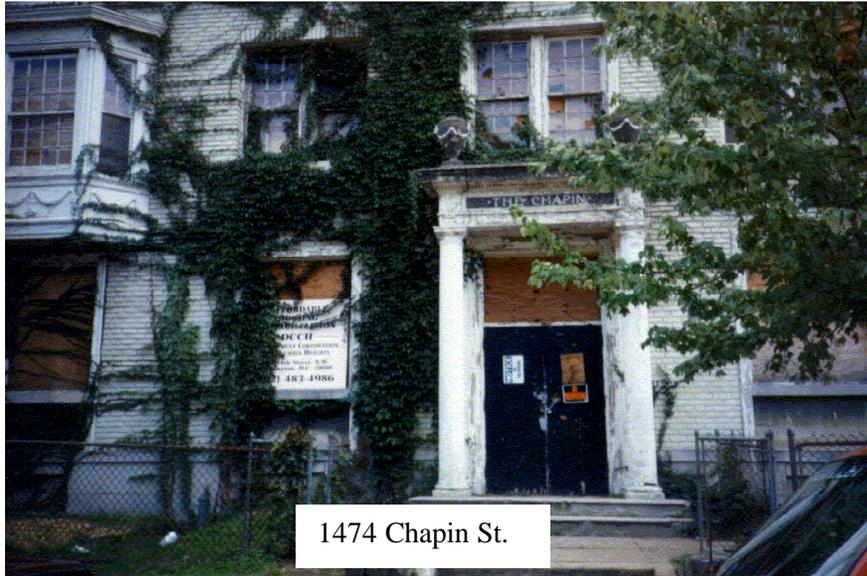
¹ Although we requested specific dates of termination, DHCD usually provided only the year of termination. DHCD provided conflicting information on Chaplin Woods.

FINDINGS AND RECOMMENDATIONS

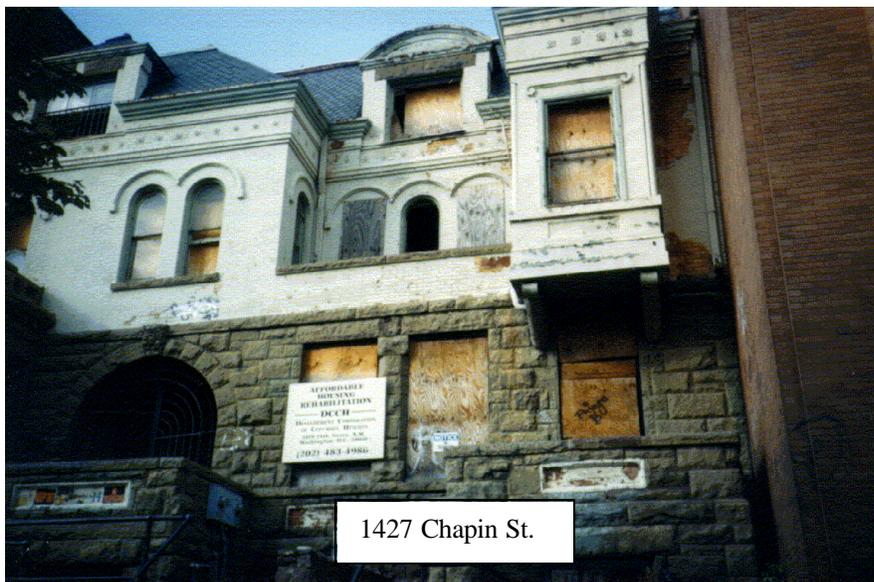
FINDING 2: Monitoring Project Performance

construction conference for November 1999 and stated that financing was in place to start construction. The project, located in the Northwest quadrant of the District, had been funded administratively for 4 years and was estimated to cost \$1,864,627 to complete.

1474 and 1427 Chapin Street, and 1030-1034 Euclid Street, N.W Projects. DHCD stated that these three projects were "...included in the bundling of projects in a demonstration being carried out by the District's Housing Finance Agency. The projects will receive Low Incoming Housing Tax Credits and Tax Exempt Bond financing and is moving through the approval process. The process has been lengthy, but final approvals are expected soon."



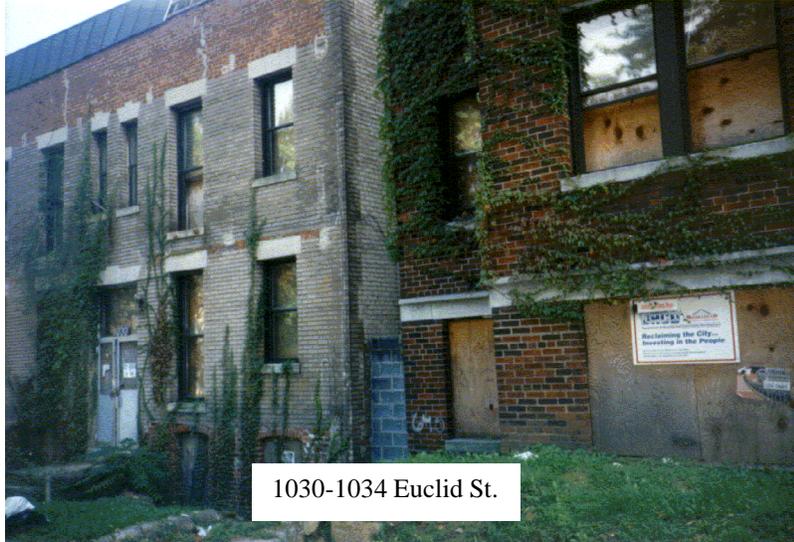
Available estimates showed that the 1474 Chapin Street project, located in the Northwest quadrant of the District, would cost \$1,600,000, which entails renovating this apartment building. DHCD provided administrative funding for 2 years, fiscal year 1998 through 1999.



Available estimates showed that this project, also located in the Northwest quadrant of the District, would cost \$1,630,000, which entails rehabilitating this apartment building. DHCD provided administrative funding for 2 years, fiscal year 1998 through 1999.

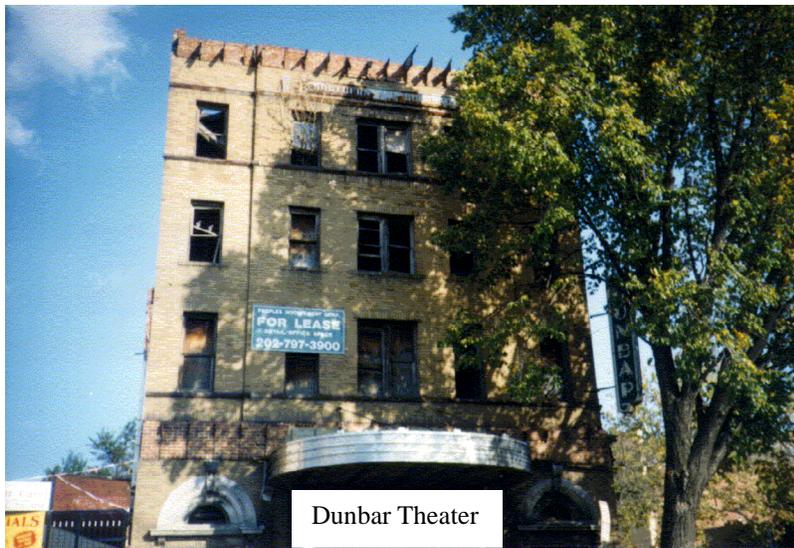
FINDINGS AND RECOMMENDATIONS

FINDING 2: Monitoring Project Performance



Located in the Northwest quadrant of the District, this project was expected to cost \$1,708,318 to complete the rehabilitation of this apartment building. DHCD provided administrative funding for 3 years, from fiscal year 1996 through 1998.

Dunbar Theater. The Dunbar Theater is located on 7th Street in Northwest. The project entails renovating the Theater at a cost of \$1,960,000, and DHCD provided administrative funds



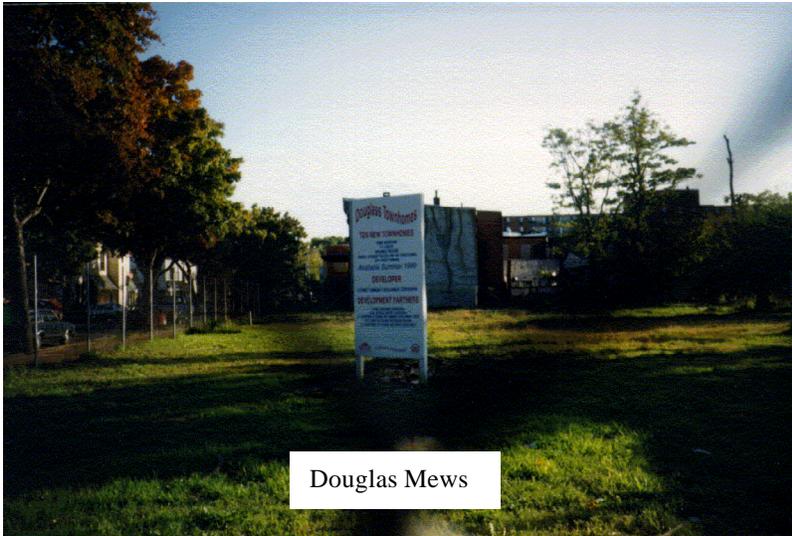
on subgrants for the project for 5 years, fiscal year 1995 through 1999. DHCD stated that this project:

...has taken some time for basically two reasons, mainly the lack of parking associated with the building and the fact that the type of tenants interested in developing the building have been not compatible with the goals of the community surrounding the building. The developer now has a proposal from business to lease the entire building. The developer is now in lease negotiations with the prospective tenant.

FINDINGS AND RECOMMENDATIONS

FINDING 2: Monitoring Project Performance

Douglass Mews Housing Project. This housing project is located in the District's Northeast area and funds ten new townhouses as affordable homeownership.



Project costs were expected to total \$1.5 million. DHCD has provided administrative funds for 3 years, fiscal year 1997 through 1999.

We question the \$3,556,000 spent on 14 projects. The eight terminated projects and the six projects pictured in the preceding paragraphs suggest that little effort and progress have been made over the years although funds were provided by DHCD to CDCs to get these projects moving. DHCD had not captured or allocated the costs of such activities to projects. Accordingly, we estimated the average administrative costs for each project to be about \$254,000, which is the total value of the subgrants funding the 74 projects (\$18.8 million) divided by the number of administratively funded projects.

RECOMMENDATION 2

We recommend that the Director, DHCD:

- a. Develop, document, and implement procedures and controls for the Developmental Finance Division to ensure that projects are routinely and continuously monitored throughout the life of each project.
- b. Develop a standardized monitoring report for the Developmental Finance Division that will capture and document activities and accomplishments of CDBG funded recipients that will also measure progress against goals and milestones;
- c. Allocate adequate resources to the Residential and Community Services Division so that all administrative subgrant recipients and related projects are monitored; and
- d. Obtain and provide to the Office of the Inspector General supporting documentation for the eight terminated projects and the six “pictured” projects that shows what was accomplished, related reports, and other documentation that shows what was spent on each project.

FINDINGS AND RECOMMENDATIONS

FINDING 2: Monitoring Project Performance

DHCD RESPONSES

Recommendation 2.a. As a result of management reform effort undertaken by DHCD, new procedures were put in place for the Development Finance Division's funding process. Procedures for monitoring recipients of funding for housing and community development projects are being developed. Target date to complete planned actions is April 30, 2000.

Recommendation 2.b. An integral part of the new monitoring procedures is the "Project Monitoring Checklist," which is to be completed each time a monitoring activity takes place on a project. This aspect will be discussed as part of the monitoring process to be developed. Target date to complete planned actions is April 30, 2000.

Recommendation 2.c. DHCD will initiate the actions to allocate the necessary resources to the Residential and Community Services Division. This action involves requesting the Chief Financial Officer, the Mayor, and the Financial Authority to approve an increase in DHCD's full time equivalents.

Recommendation 2.d. DHCD states that actual costs for administratively funded projects during the audit period could not be determined because the administrative cost incurred under the subgrant to the CDC was not intended solely for project development. It should be noted that the pictures in the report do not show what was accomplished with DHCD's administrative funds. Administrative funds were provided to pay for staff work on the project. It does not fund the actual development of the project.

OIG COMMENTS

The action planned by DHCD for recommendations 2.a., 2.b., and 2.c. should correct the conditions noted. However, in regard to DHCD's response to recommendation 2.c., DHCD should ensure that other staff resources within DHCD are fully and appropriately utilized before seeking additional full time equivalent positions.

For recommendation 2.d., DHCD can not provide actual costs for administratively funded projects during the audit period because administrative cost incurred under the subgrant to the CDC was not intended solely for project development. Further, the CDCs were not required to track costs in that manner. However, DHCD's response to recommendations 3.a. and 3.b. indicate that DHCD initiated procedures that require the CDC's to track the administrative costs for projects and other activities funded by subgrants. We believe that DHCD's action should provide accountability and visibility of project and other administrative costs in the future.

FINDINGS AND RECOMMENDATIONS

FINDING 3: ACCOUNTABILITY FOR ADMINISTRATIVELY FUNDED PROJECTS

SYNOPSIS

DHCD did not record or track by project the amount of funds expended for the administrative costs for at least 74 projects undertaken by the CDCs during fiscal years 1994 through 1999. DHCD paid the CDCs for vouchers submitted by the CDCs without requiring the CDCs to account for the funds spent on the projects. As a result, DHCD could not substantiate that the \$23.1 million it had awarded by subgrants to the CDCs was spent or will be spent for the purposes contained in the authorizing subgrants and the purposes of CDBG funds. In addition, we can not determine whether the total direct and indirect costs of a project, funded with CDBG funds, were correct.

AUDIT RESULTS

DHCD's Residential and Community Services Division had cognizance over the administrative subgrant agreements under the Neighborhood Development Assistance Program (NDAP), a program funded by CDBG funds. These "administrative" subgrants funded only the pre-construction costs of projects (and non project efforts) whose actual physical development costs were funded by non-District Government funds or were expected to be funded with other subgrants or loans issued under the cognizance of DHCD's Development Finance Division, also using CDBG funding. This finding does not include the subgrants under the cognizance of the Development Finance Division for the direct costs of projects.

DHCD awarded 54 subgrant agreements, totaling \$23.1 million to the CDCs during FY 1994 through FY 1999 that authorized the CDCs to incur administrative costs related to Neighborhood Development Projects and Neighborhood Revitalization Activities. However, as also discussed in Finding 2, "Monitoring Project Performance," DHCD did not provide 11 of those subgrant agreement documents, totaling \$4.3 million, for our review. Accordingly, we were unable to determine the total number of Neighborhood Development Projects funded by those 54 subgrant agreements. We reviewed, in detail, the 43 subgrant agreements, totaling \$18.8 million, that DHCD made available. Neither DHCD nor the CDCs accounted for the costs of specific Neighborhood Development Projects and Neighborhood Revitalization Activities.

Each administrative subgrant agreement required the CDCs to undertake specific Neighborhood Development Projects, 74 specific projects for the 43 subgrant agreements we reviewed in detail (see Exhibit 8).

Subgrant Agreements. The administrative subgrants that DHCD issued to the CDCs each contained a provision similar to that contained in the FY 1998 subgrant agreement, CD-9801. In Section I., "Scope of Services," paragraph I.A.2 stated, "The GRANTEE [subgrantee] shall complete the projects listed below. This [effort] shall be accomplished by

FINDINGS AND RECOMMENDATIONS

FINDING 3: Accountability for Administratively Funded Projects

undertaking administrative and technical activities....” The projects were also identified in the Work Plans, Attachment B to the contracts. The projects were identified as:

- Anacostia Northern Gateway
- Good Hope Market Place
- Martin Luther King Development
- Hillsdale Walk Townhouses
- Bolling View Demonstration Program
- Skyland Shopping Center

Tracking Administrative Costs. The subgrants DHCD issued to the CDCs contained no requirement to track costs by project. Accordingly, neither the CDCs nor DHCD could determine how much of the administrative costs were related to each project. Instead, the CDCs submitted vouchers that classified costs, as directed by the subgrant, in categories, such as:

- Personnel
- Consultants & Contract Services
- Travel
- Space
- Consumable Supplies
- Rental, Lease, Purchase of Equipment
- Insurance

Such categories provided no insight into the costs of the projects that were funded. DHCD reviewed the vouchers and approved the vouchers for payment, although the relationship of these costs to the projects was never established. Our visits to the CDCs and discussions with CDC officials showed that they had no tracking system or allocating methodology in place to relate the costs to the specific projects.

Title 24 , Subtitle B, of the Code of Federal Regulations, “Regulations Relating to Housing and Urban Development. Recipients of CDBG funds, are required by 24 CFR, §570.506, to establish and maintain sufficient records to provide a full description of each activity assisted with CDBG funds. The records should include the amount of CDBG funds budgeted obligated and expended for each activity. In addition, §85.20, requires the recipient and the subrecipient to maintain records which contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income

DHCD officials agreed that the amount of funds expended for pre-construction activities for each of the 74 projects undertaken by the CDCs were not recorded or tracked by project. However, for subgrants issued in FY 2000, a DHCD official informed us that CDCs will be required to submit an administrative budget for each project and maintain records to summarize the amount of expenditures for each of the projects.

FINDINGS AND RECOMMENDATIONS

FINDING 3: Accountability for Administratively Funded Projects

Conclusion. Costs charged to these administrative subgrants by the CDCs were for its personnel, consultants and contracts, space, travel, consumable supplies, insurance, and the rental, lease or purchase of equipment. It would appear that the funds were used to operate the CDCs. Arguably, one could classify the full amount of administrative costs awarded to the CDCs from FY 1994 through FY 1999 as questioned costs because the CDCs did not, and were not required by their subgrant to, specifically relate the costs to the projects. While we believe this condition is a serious concern for the 6 fiscal years we audited, more importantly, DHCD needs to correct the process for future grants and subgrants it will award. While DHCD's plans for its FY 2000 and subsequent grants intend to require the CDCs to budget for project costs, DHCD did not inform us on how it intended the CDCs to track or allocate costs to the projects. Also, DHCD has not formalized the process it intends to use in mandatory procedure instructions or manuals.

RECOMMENDATION 3

We recommend that the Director, DHCD:

- a. Establish procedures and controls that ensure DHCD awards its grants and subgrants with provisions requiring CDCs and other grant and subgrant recipients to track administrative costs by project; and
- b. Ensure the CDCs and other recipients of DHCD grants or subgrants awarded in FY 2000 and subsequent years, have an adequate cost tracking or allocation process in place before paying vouchers for administrative costs.

DHCD RESPONSES

Recommendation 3.a. DHCD concurs with the recommendation and included requirements to track administrative costs tied to projects and to other activities funded by subgrants. Fiscal year 2000 solicitations and resulting grants include these requirements. Actions are completed.

Recommendation 3.b. DHCD does not concur with the recommendation. The cost categories currently used are required in keeping with the use of administrative funds. Therefore, DHCD will continue to use the cost categories as they currently exist in the subgrants.

OIG COMMENTS

The action completed by DHCD, in response to recommendation 3.a., should allow for visibility and accountability of project costs. It's encouraging that DHCD initiated corrective action before our audit was completed.

DHCD's lack of concurrence for recommendation 3.b. is noted. However, DHCD's actions in response to recommendation 3.a. provided the necessary visibility, accountability, and

FINDINGS AND RECOMMENDATIONS

FINDING 3: Accountability for Administratively Funded Projects

insight into project costs for FY 2000 subgrants and should associate costs with accomplishments. We are puzzled by the lack of concurrence with recommendation 3.b. that recommended having the system (recommendation 3.a.) in place before making payments. Documentation submitted indicates that the CDCs will track by project. Accordingly, we believe that DHCD took appropriate action based on its response to recommendation 3.a. and consider action completed and subject to follow-up reviews at a later date.

FINDINGS AND RECOMMENDATIONS

FINDING 4: EXPENDITURES FOR CDBG ACTIVITIES

SYNOPSIS

DHCD authorized expenditures totaling \$12,850,000 for two projects, which includes \$11,745,000 that we consider questioned costs because DHCD did not provide to us sufficient documentation for review. As a result, we were unable to review expenditures for the Good Hope Marketplace Place Project (\$11.5 million) and the New York Avenue Metrorail Feasibility Station Study (\$245,000) to determine compliance with CDBG regulations and grant provisions.

AUDIT RESULTS

Recipients of CDBG funds are required by Title 24 CFR, §570.506, to establish and maintain sufficient records to provide a full description of each activity assisted with CDBG funds. The records should include the amount of CDBG funds budgeted, obligated, and expended for each activity. In addition, §85.20, requires the recipient and the subrecipient to maintain records which contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income. Accordingly, DHCD should be able to readily make such information available for audit in connection with the activities it funds with CDBG funds, such as the Good Hope Marketplace Project and the New York Avenue Metrorail Feasibility Station Study.

The Good Hope Marketplace Project. DHCD provided a subgrant of CDBG funds, totaling \$12.5 million, to a “CDC affiliate” to fund the acquisition of the Good Hope Marketplace Shopping Center. The subgrant included funding under the Section 108 Loan Guarantee program; this Section enables states and local governments participating in the CDBG program to obtain federally guaranteed loans for large economic development projects and other revitalization activities. In this regard, DHCD submitted an application to HUD under the Section 108 Loan Guarantee program for \$11.5 million, which was approved on March 5, 1995, to fund the acquisition and management of the shopping center. DHCD also received an Economic Development Initiative grant in the amount of \$1 million for this project.

On October 27, 1999, we formally requested DHCD to provide a schedule showing how the \$12.5 million was used. Specifically, we asked DHCD to provide a schedule showing to whom the funds were disbursed, dates of disbursement, and amounts. As of the date of this report, DHCD has provided supporting information for only \$1 million of the \$12.5 million involved. As a result, we can not determine whether the funds were disbursed in accordance with CDBG regulations and in compliance with the applicable grant provisions.

The New York Avenue Metrorail Feasibility Station Study. DHCD provided a subgrant of CDBG funds to a provider, totaling \$350,000, to complete this study. In response to our request for documentation to support the expenditures, DHCD provided available records

FINDINGS AND RECOMMENDATIONS

FINDING 4: Expenditures for CDBG Activities

that adequately supported payments of only \$105,000. DHCD, in response to our request, asked the involved subcontractor to provide additional information, which DHCD provided to us. However, the information provided to us was primarily printouts of labor hours per person and lacks rates and other information to support the expenditure. Furthermore, DHCD did not provide timesheets to support the printouts. Accordingly, we were unable to assure ourselves that funds were used for the purpose intended by regulations and grant provisions.

RECOMMENDATION 4

We recommend that the Director, DHCD, provide the documentation to support the disbursements made for the Good Hope Marketplace Project and the New York Avenue Metrorail Feasibility Station Study.

DHCD RESPONSE

DHCD provided memoranda, settlement sheets, and other information to support the propriety of disbursements and amounts of disbursements. The funds were expended for the intended purpose of the HUD 108 loan, and the Good Hope Marketplace continues to be a fully functioning community retail center. Through verification of documentation submitted, DHCD was assured that the funds provided for the New York Avenue Metrorail Feasibility Station Study were expended in accordance with the grant provisions and program regulations.

OIG COMMENTS

DHCD was not responsive to the recommendation and has yet to show sufficient documentation to support disbursements, totaling \$11.5 million, from the District Treasury for the Good Hope Marketplace. In addition, DHCD did not show time sheets and other documents that would support the propriety of the \$245,000 it paid to a contractor in connection with the New York Avenue Metrorail Feasibility Station Study. This matter remains unresolved.

Good Hope Market Place. The OIG has repeatedly met with DHCD management and requested a schedule showing to whom the funds were disbursed, dates of disbursements, and amounts disbursed. In addition to the schedule, the OIG needs to substantiate the transactions indicated on the schedule. To date, DHCD has not provided the detailed information necessary to ensure that the funds were properly disbursed. DHCD's response indicates several wire transfers of funds, yet it provided evidence for only \$1 million.

New York Avenue Metrorail Feasibility Station Study. Notwithstanding, DHCD's assurance that funds were expended in accordance with the grant provisions and program regulations, its evidence is insufficient. We have repeatedly requested timesheets and other documentation to support expenditures totaling \$245,000.

FINDINGS AND RECOMMENDATIONS

FINDING 5: FINANCIAL DISCLOSURE OF EMPLOYEES

SYNOPSIS

The District of Columbia Personnel Manual (DPM) provides controls for assuring that District employees avoid conflicts, or the appearance of conflicts, of interest. At DHCD, however, these controls had become largely a paper exercise because employees did not always identify their financial interests, reviewers did not seek sufficient additional information to make sound decisions when employees have identified financial interests, and employees did not always file their financial disclosures on time. Controls have been ineffective because the District-wide financial disclosure forms contained language that could be improved to elicit required information, instructions were complicated, and neither the employees nor those who reviewed the disclosures and managed the disclosure process had an adequate understanding of the DPM requirements. As a result, the calendar year (CY) 1998 annual financial disclosures were ineffective, and the recent CY 1999 annual financial disclosures may have been ineffective in disclosing or resolving conflicts or potential conflicts of interest of DHCD employees.

AUDIT RESULTS

The DPM, Chapter 18, Section 1813, provides for agencies to designate employees who shall submit Confidential Statements of Employment and Financial Interests, DC Form 35. Such designated employees shall submit these statements no later than May 15th of each year, and the agency head or his or her designee shall review these statements to identify and resolve conflicts or apparent conflicts of interest no later than June 15th of each year. In addition, employees are required to file the statement within 10 days after their position is determined to meet the reporting requirements and after appointment, transfer, promotion, or detail to a position covered by the reporting requirements. Employees are also required to keep the information on the statement current with respect to all categories and shall obtain prior approval from the agency head or his or her designee before engaging in outside employment or business activities.

The DPM requires designated employees to consider the interest of a member of the employee's immediate household to be the interest of the employee. The employee (for the household members) shall identify the names and addresses of all corporations, companies, or other business enterprises, partnerships, nonprofit organizations, and educational or other institutions in any instance when the District employee (household members): is an employee, officer, owner, director, member, trustee, partner, advisor, or consultant; has a continuing financial interest through a pension or retirement plan, shared income, or other arrangement as a result of any current or prior employment or business or professional association; or has any financial interest through the ownership of stock, stock options, bonds, securities or other arrangement, including trusts. The employee is also required to identify information about certain creditors and about real property other than a personal residence.

FINDINGS AND RECOMMENDATIONS

FINDING 5: Financial Disclosure of Employees

Identifying Financial Interests. DHCD'S process for determining the existence of conflicts of interest had not worked effectively because its employees had not always identified their complete financial interests. Employees subject to identifying financial interests had sometimes omitted their own financial information and the financial interests of members of their household. Employees did not carefully read the form and its directions and had no training in completing the form. In CY 1999, DHCD identified 81 of its 111 personnel as subject to filing disclosure statements; however, for CY 1998 and 1999, it was largely a paper exercise. As a result, management could not be assured that conflicts or the appearance of conflicts were resolved in accordance with the DPM.

We selected 21 disclosure statements filed in CY 1998 for review; only 6 employees disclosed financial interests. Accordingly, we interviewed 10 employees to determine whether they understood the DPM requirements. These interviews showed: (1) All 10 employees received the applicable portions of DPM, Chapter 18, but received no oral guidance. (2) Only 2 employees understood that they should have been reporting financial interests of their household. None of the married employees, with working spouses, reported their spouse's employment; 6 spouses worked. (3) Of the 10 employees, 6 disclosed either stocks, mutual funds, retirement holdings, rental property, associations, or businesses not disclosed on the DC Form 35. (4) Overall, 9 of 10 employees did not understand the guidance and 8 did not completely disclose financial interests. (5) All 10 employees commented on the complex guidance of the DPM and the word choices used in the design of DC Form 35. For example, Section I of this form specifically provides: "List the names of all business enterprises ...with which **you** are connected as an employee...." Bolding added to emphasize that employees could overlook reporting requirements based on the form's word choice. In contrast, Section II refers to "your immediate household."

Reviewing Financial Interests. After the employee certified the DC Form 35, the DHCD reviewing official was required to evaluate the employee statements to ensure actual and apparent conflicts of interest were avoided. However, we saw insufficient evidence that an informed decision could be made in the 6 instances in which employees reported financial interests. For example, in one instance the employee reported having rental property. The reviewer did not ask for additional information to determine to whom the property was rented; yet the reviewer's evaluation was "Reported affiliation/financial interests are unrelated to assigned or prospective duties, and no conflicts appear to exist." In addition, reviewing authorities should have noticed the DHCD-wide lack of financial interests reported.

Filing Timely Financial Disclosures. DHCD lacked controls to ensure personnel, who occupy designated positions, timely file required disclosure statements at times other than the annual District-wide action. DHCD did not track the positions subject to filing and relied upon supervisors at the time of the annual disclosure process to identify personnel who were subject to filing the disclosure statements. As a result, DHCD did not timely obtain disclosure statements from personnel who were appointed or detailed to a position, transferred or promoted into a position, or whose position became subject to reporting.

FINDINGS AND RECOMMENDATIONS

FINDING 5: Financial Disclosure of Employees

DHCD Action. We advised the Director, DHCD, by Management Alert Report on May 10, 1999 (Exhibit 1) of the need to make immediate corrections to its financial disclosure process in order to have an effective process and still meet its reporting deadlines. In response to that Management Alert Report and our recommendations, DHCD:

1. Scheduled a training session for its employees to go over the preparation of the financial disclosure statement and to provide an overview of the DPM, Chapter 18, Section 1813. The Ethics Counselor for the District Government was expected to be in attendance at the training session to answer questions and provide clarification.
2. Intended to reissue the Financial Disclosure forms after the training with an expedited turnaround time for completion.
3. Designated the Office of Corporation Counsel to serve as the reviewer of the financial disclosure statements.
4. Notified the District Ethics Counselor of the findings related to the financial disclosure statements.
5. Intended to meet the June 15th deadline.
6. Established a list of positions subject to the financial reporting process and track those positions as they are filled to ensure timely filing of financial disclosure statements.

RECOMMENDATION 5

We recommend that the Director, DHCD:

- a. Reinitiate the calendar year 1999 annual financial disclosure process after training employees, who are in positions designated to file disclosure statements, in the requirements of the DC Personnel Manual, Chapter 18;
- b. Require employees involved in the review process to obtain sufficient additional information before evaluating employee disclosure statements; and
- c. Establish and track positions subject to filing disclosure statements to ensure that employees who fill these positions file disclosure statements within 10 days.

DHCD RESPONSES AND OIG COMMENTS

We summarized the DHCD response (Exhibit 2) to the Management Alert Report in the finding. DHCD's actions should resolve the conditions noted and actions are complete on the three recommendations made in Exhibit 1 and which are repeated in the previous paragraph for

FINDINGS AND RECOMMENDATIONS

FINDING 5: Financial Disclosure of Employees

tracking and follow-up purposes. Recommendation 5.b. was not specifically addressed. Nonetheless, we consider action for recommendation 5.b. to be completed because responsibility for the review of DHCD financial disclosure statements now resides in the Office of Corporation Counsel, which is also responsible for District-wide implementation of financial disclosure reporting.

FINDINGS AND RECOMMENDATIONS

FINDING 6: CONTROLS OVER CONFLICT OF INTEREST AT COMMUNITY DEVELOPMENT CORPORATIONS

SYNOPSIS

The CDCs did not have adequate controls and procedures to prevent and detect conflicts of interests by the officers, board members, and employees. DHCD had not included within its subgrant agreements and loans to the CDCs a specific requirement for conflicts of interest. Only one CDC had a system, procedures, or other means to monitor or detect conflicts of interests by its officers and employees. As a result, we could not be assured that the CDCs used CDBG funds in the most judicious manner, uninfluenced by personal financial interests of CDC board members, officers, and employees.

AUDIT RESULTS

Our tests showed that none of the eight CDCs we visited had adequate procedures to prevent or detect conflicts of interest. Only five CDCs had procedures regarding conflicts of interest but generally addressed only employee conduct; three CDCs had no procedures. Also, an audit of one CDC, conducted under the authority of OMB Circular A-133, showed that the CDC had created and held ownership or partial ownership in many profit making affiliates. Our review showed the CDC and the profit making affiliates sometimes shared the same corporate officers. This CDC awarded loans of CDBG funds to its affiliate profit-making entities. In our opinion, the transactions lack the appearance of “arm’s length transactions,” which is so necessary to avoid the appearance of gains from inside information. Our effort to determine the extent that other CDCs were involved in similar situations was suspended pending resolution of the propriety of this CDC’s transactions, which remains under review. DHCD were aware of some of these transactions, but we are unsure the extent that DHCD knew of the financial relationships of the CDC, its board members, officers, employees, and affiliates.

Available CDC Conflict of Interest Procedures. Each CDC was asked for its procedures to control, prevent, or detect conflicts of interests within their organizations. Procedures were available for five CDCs, two had none, and one CDC claimed to have such procedures but didn’t provide them to us.

Inadequacy of CDC Procedures. A comparison of CDC standards of conduct with regulatory requirements for such procedures showed that existing CDC procedures were inadequate when CDBG funds were involved. Table B provides a few examples in which the CDCs were inadequate in addressing regulatory requirements.

FINDINGS AND RECOMMENDATIONS

FINDING 6: Controls Over Conflict of Interest at Community Development Corporations

Table B: Omitted Regulatory Requirements in CDC Procedures

Omission	Community Development Corporations ²							
	1	2	3	4	5	6	7	8
Written Conduct Standards			X				X	X
Discipline for Violations	X			X	X	X		
Address Officers & Agents and Contractors & Their Agents	X	X		X	X	X		
“Apparent” Conflicts		X		X		X		
Applicability of Restrictions After Leaving the CDC	X	X		X	X	X		

Table B summarizes and quantifies the specific types of omissions and deviations from regulatory requirements. Our review and comparison of available CDC conflict of interest procedures disclosed that none of the available CDC’s written conduct standards clearly and explicitly met the regulatory requirements, which intends for officers and employees, agents, and consultants to know that those with inside information, and family members, should not have any financial interest in activities benefiting from CDBG funds.

Two CDCs had within its written standards a requirement that could be interpreted by the CDC employee differently than the regulatory requirements. The two CDCs provided that, “Employees will not solicit or receive anything of value, including gifts, favors, services, loans, gratuities, discounts, hospitality, contributions, or promises of future employment as inducements to do or continue business.” Underlining added to recognize that regulatory requirements preclude receiving such items, in most cases, regardless of the intent of the employee or the person offering the item of value.

One CDC, while having the most comprehensive written procedures involving conflict of interest, clearly had procedures that did not meet the intent of 24CFR§570.611(b) that precludes those with inside information from having any financial interest in activities benefiting from CDBG funds.

² The specific Community Development Corporation is identified only as a number for illustration purposes. The specific information has been made available to DHCD, but is not available for public release.

FINDINGS AND RECOMMENDATIONS

FINDING 6: Controls Over Conflict of Interest at Community Development Corporations

Regulatory Requirements. Title 24 CFR §84.42, §85.36, and §570.611 impart conflict of interest provisions for organizations receiving CDBG funds.

§570.611

(a) Applicability.

(1) In the procurement of supplies, equipment, construction, and services by recipients and by subrecipients, the conflict of interest provisions in 24 CFR 85.36 and 24 CFR 84.42, respectively, shall apply.

(2) In all cases not governed by 24 CFR 85.36 and 84.42, the provisions of this section shall apply. Such cases include the acquisition and disposition of real property and the provision of assistance by the recipient or by its subrecipients to individuals, businesses, and other private entities under eligible activities that authorize such assistance (e.g., rehabilitation, preservation, and other improvements of private properties or facilities pursuant to Sec. 570.202; or grants, loans, and other assistance to businesses, individuals, and other private entities pursuant to Sec. 570.203, 570.204, 570.455, or 570.703(i)).

(b) Conflicts prohibited. The general rule is that no persons described in paragraph (c) of this section who exercise or have exercised any functions or responsibilities with respect to CDBG activities assisted under this part, or who are in a position to participate in a decisionmaking process or gain inside information with regard to such activities, may obtain a financial interest or benefit from a CDBG-assisted activity, or have a financial interest in any contract, subcontract, or agreement with respect to a CDBG-assisted activity, or with respect to the proceeds of the CDBG-assisted activity, either for themselves or those with whom they have business or immediate family ties, during their tenure or for one year thereafter. For the UDAG [Urban Development Action Grants] program, the above restrictions shall apply to all activities that are a part of the UDAG project, and shall cover any such financial interest or benefit during, or at any time after, such person's tenure.

(c) Persons covered. The conflict of interest provisions of paragraph (b) of this section apply to any person who is an employee, agent, consultant, officer, or elected official or appointed official of the recipient, or of any designated public agencies, or of subrecipients that are receiving funds under this part.

§85.36.b.(3) Procurement.

Grantees and subgrantees will maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. No employee, officer or agent of the grantee or subgrantee shall participate in selection, or in the award or administration of a contract supported by Federal funds if a conflict of interest, real or apparent, would be involved. Such a conflict would arise when: (i) The employee, officer or agent, (ii) Any member of his immediate family, (iii) His or her partner, or (iv) An organization which employs, or is about to employ, any of the above, has a financial or other interest in the firm selected for award. The grantee's or subgrantee's officers, employees or agents will neither solicit nor accept gratuities, favors or anything of monetary value from contractors, potential contractors, or parties to subagreements. Grantee and subgrantees may set minimum rules where the financial interest is not substantial or the gift is an unsolicited item of nominal intrinsic value. To the extent permitted by State or local law or regulations, such standards or conduct will provide for penalties, sanctions, or other disciplinary actions for violations of such standards by the grantee's and subgrantee's officers, employees, or agents, or by contractors or their agents. The awarding

FINDINGS AND RECOMMENDATIONS

FINDING 6: Controls Over Conflict of Interest at Community Development Corporations

agency may in regulation provide additional prohibitions relative to real, apparent, or potential conflicts of interest.

§84.42 Codes of conduct.

The recipient shall maintain written standards of conduct governing the performance of its employees engaged in the award and administration of contracts. No employee, officer, or agent shall participate in the selection, award, or administration of a contract supported by Federal funds if a real or apparent conflict of interest would be involved. Such a conflict would arise when the employee, officer, or agent, any member of his or her immediate family, his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in the firm selected for an award. The officers, employees, and agents of the recipient shall neither solicit nor accept gratuities, favors, or anything of monetary value from contractors, or parties to subagreements. However, recipients may set standards for situations in which the financial interest is not substantial or the gift is an unsolicited item of nominal value. The standards of conduct shall provide for disciplinary actions to be applied for violations of such standards by officers, employees, or agents of the recipient.

Detecting Conflicts of Interest. Regulatory requirements do not require, as do District regulations for District employees, a means for the CDC employee to identify financial interests and holdings. Accordingly, the CDCs and other recipients of DHCD subgrants are not required to have their officers, board members, and employees disclose their financial interest for review. In our opinion, controls over conflict of interest are handicapped by lack of such disclosure. We are unaware of any restriction that would prevent DHCD from strengthening conflict of interest controls by requiring its subgrant and loan recipients to establish a process for disclosing and analyzing financial interests for CDC officers, employees, and their family members. Without this requirement in DHCD subgrant and loan provisions, the detection of real or apparent conflicts of interest by a CDC or DHCD are severely hampered.

At least one CDC had, within its written standards of conduct, a requirement for disclosing “any interest and/or associations with any persons, associations, and organizations applying for or receiving assistance, in any manner, from the Corporation.” However, the requirement did not disclose the process used to identify such interests and associations. Another CDC, however, required annual and supplemental disclosure statements for its officers and directors. The Executive Director and Secretary were required to review the statements and convey perceived conflicts of interest to the attention of the Board of Directors.

RECOMMENDATION 6

We recommend that the Director, DHCD:

a. Include a requirement within subgrant and loan agreements that ensure CDCs and other recipients of CDBG funds have written standards of conduct that address all applicable elements of Title 24, Sections 570.611, 85.36.b.(3), and 84.42; and

b. Include a requirement within subgrant and loan agreements that ensure CDCs and other recipients of CDBG funds require employees, officers, and board members to submit annual and

FINDINGS AND RECOMMENDATIONS

FINDING 6: Controls Over Conflict of Interest at Community Development Corporations

supplemental statements of financial interests for review by appropriate recipient officials to detect potential conflicts of interest.

DHCD RESPONSES

Recommendation 6.a. The requirement is included in all FY 2000 subgrant agreements. DHCD will ensure that all CDC and other grant recipients maintain a current conflict of interest policy consistent with 24 CFR, Parts 570.611, 85.36.b.(3), and 84.42 and that all grant subrecipients develop and implement administrative controls to prevent and detect employee conflicts of interest. Action is completed.

Recommendation 6.b. DHCD will amend FY 2000 subgrants to require CDCs to provide annual statements of financial interests for employees, officers, and board members for review by DHCD personnel. These statements will be due 30 days after execution of the amendment, and on an annual basis, thereafter. DHCD will review these statements to ensure that conflicts of interest or the appearance thereof do not exist. For all other subrecipient agreements, DHCD staff will ensure that employees of subrecipients have complied with the conflict of interest provision, and that management has reviewed employee disclosure statements. Target date is March 31, 2000.

OIG COMMENT

The actions completed and planned by DHCD should correct the conditions noted.