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August 31, 2009

**MEMORANDUM NO**:
2009-FW-1802

**MEMORANDUM FOR:** Katie S. Worsham
Director, Office of Community Planning and Development, 6AD

*//signed//*
**FROM:** Gerald R. Kirkland
Regional Inspector General for Audit, Fort Worth Region, 6AGA

**SUBJECT:** The City of Fort Worth, Texas, Needs to Strengthen Its Capacity to Adequately Administer Recovery Funding

## INTRODUCTION

The City of Fort Worth (City) is scheduled to receive $10.85 million under the Housing and Economic Recovery Act of 2008 (HERA) and the American Recovery and Reinvestment Act of 2009 (ARRA). These Acts require swift obligation and expenditure deadlines with stringent emphasis on accountability and transparency. As part of our organization's commitment to ensure the proper use of these funds, we performed a review of the City's operations to evaluate its capacity to administer HERA and ARRA funding. Specifically, our objective was to review and assess the City's capacity and risks in the following areas: basic internal controls, financial operations, and procurement.

We provided a draft report to the City on July 28, 2009, and received written comments on August 11, 2009. We have included the comments and our evaluation of those comments in appendix B.

For each recommendation without a management decision, please respond and provide status reports in accordance with U. S. Department of Housing and Urban Development (HUD) Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the review.

## METHODOLOGY AND SCOPE

Our review period was June 1, 2008, to May 31, 2009. Because the City continued to have several outstanding issues concerning previous HUD monitoring, financial, and action plan reviews, we expanded our review to include those matters. We conducted our review from May 11 through August 5, 2009, at the City's Housing and Economic Development Department,

908 Monroe Street; City Hall, 1000 Throckmorton Street; and a City Annex Office, 275 West 13th Street, Fort Worth, Texas.

To accomplish our objective, we

- Reviewed and obtained an understanding of HERA and ARRA legislation, relevant program guidance and criteria, the City's grant agreements with HUD, and its planned activities under HERA and ARRA.
- Interviewed HUD and City management and staff regarding the City's operations.
- Analyzed and evaluated HUD and independent auditor correspondence to the City and the City's responses.
- Reviewed City financial records and procurement files including 15 contracts totaling more than $2.7 million. The City did not maintain an accurate contract log, thereby limiting our scope. We selected contracts based upon dollar value from existing HUD-funded City programs. While this was not a statistical sample, we expect it to be representative of the City's procurement for recent activities similar to HERA and ARRA contracts.
- Made site visits to four sidewalk sites and seven houses and took pictures for planned City activities under HERA and ARRA.
- Attended and viewed City presentations and council meetings.

## BACKGROUND

Through various programs, HUD provides the City with resources to address a wide range of unique community development needs. The City Council appoints a professional city manager to administer and coordinate municipal operations and programs. The City's annual action plan updates the City's five-year consolidated plan and describes the activities budgeted under each of its programs. After a major reorganization in October 2008, the City's Housing and Economic Development Departments merged and assumed responsibility for administering the City's HUD grants.[1] Longstanding managers who were previously responsible for HUD programs either resigned or were dismissed shortly after the reorganization.

After reviewing the City's annual action plan, HUD approved the following City grants for program year 2008:[2]

[1] Before the merger, the City's Housing Department administered HUD grants.

[2] The City's program year runs from June 1 through May 31. Its fiscal year runs from October 1 through September 30.

| Program | Amount |
|---|---|
| • Community Development Block Grant | • $ 6,614,078 |
| • Emergency Shelter Grant | • 293,257 |
| • Home Investment Partnerships Program | • 2,920,630 |
| • Housing Opportunities for Persons with AIDS | • 863,000 |
| • **Total** | • **$ 10,690,965** |

In addition to its annual 2008 funding, the City received $10.85 million in HERA and ARRA funding allocations for three HUD programs:

| Program | Amount |
|---|---|
| •Neighborhood Stabilization Program (HERA funding) | • $ 6,307,433 |
| •Homelessness Prevention and Rapid Re-Housing Program (ARRA funding) | • 2,746,929 |
| •Community Development Block Grant Entitlement Grants (ARRA funding) | • 1,796,412 |
| •**Total** | • **$10,850,774** |

Moreover, the City plans to apply for more than $6 million in additional ARRA funding under HUD's Lead-Based Paint Hazard Control Grant and Lead Hazard Reduction Demonstration Grant programs. The City must expend all of its HERA and ARRA funding within 18 to 36 months after receiving it.

Under NSP, the City plans to establish a financing mechanism for the purchase and redevelopment of foreclosed homes and residential properties for low- and moderate-income home buyers through its proposed down-payment assistance program. Two months into its Neighborhood Stabilization Program (NSP), the City had expended $9,205 in administrative costs with no funds expended on its plan activities. For its Homelessness Prevention and Rapid Re-Housing Program (HPRP), the City plans to use its funding for financial assistance and housing relocation/stabilization services through eligible activities approved by HUD.[3] The City plans to use its Community Development Block Grant Entitlement Grant (CDBG-R) funds to provide sidewalk infrastructure in eligible census tracts/block groups.

[3] HUD's "Notice of Allocations, Application Procedures, and Requirements for Homelessness Prevention and Rapid Re-Housing Program Grantees under the American Recovery and Reinvestment Act of 2009," dated March 19, 2009, details eligible program activities.

Due to the City's history of unsatisfactory performance in the Community Development Block Grant and HOME Investment Partnerships programs, HUD considered the City "high risk" and placed special conditions on its approval of the City's $6.3 million NSP grant. HUD required the City to submit documentation describing how past performance and audit issues had been resolved or were being resolved and explaining how those issues would not impact administration of the City's NSP program. HUD also required the City to identify the steps it would take to ensure that all NSP activities were eligible, that the program would comply with all applicable requirements and meet a national objective. Further, the City had to detail how its NSP activities would be monitored.

## RESULTS OF REVIEW

The City had a history of failing to meet regulatory requirements in an efficient or timely manner. It acknowledged past problems and a lack of specific policies which it must address to realize successful HERA and ARRA program outcomes. Further, data that the City used to monitor its use of NSP funds contained inaccuracies. The City needs to improve its procurement activities and undertake only prudent projects.

*The City Had a History of Failing to Meet Regulatory Requirements*

When HUD attached special conditions to the City's NSP grant agreement, it specifically cited monitoring review letters, dated April 23 and May 15, 2007. In total, the two monitoring reviews reported 32 findings and 16 concerns[4] and substantial amounts of questioned costs. HUD's monitoring reviews identified serious deficiencies in the City's administration of its affordable housing programs. HUD opined that resolving these findings would require a significant commitment of staff and management resources and a change in the City's business practices. It encouraged the City to undertake these efforts in a manner that would have a lasting impact on program operations. HUD provided the City with more than 10 letters responding to additional information the City provided to address the findings. Several of the letters cited the City's failure to provide a response to HUD or reimburse its programs. As of May 27, 2009, 15 of the 32 findings remained open.

In addition to its monitoring review findings, HUD had recurring concerns regarding the City's fiscal years 2007, 2008, and 2009 action plan submissions. HUD repeatedly warned the City that its failure to take corrective action would result in delayed funding approval. Despite this knowledge, HUD agreed to approve the fiscal year 2009 action plan if the City provided written assurances that it would make corrections and complete the citizen participation process. The City met HUD's demand by providing written assurances by the required deadline.

The City's audited financial statements detailed multiple findings and deficiencies from 2004 to 2007. Further, the audited financial statements were submitted late each of the last four years, ranging from 16 to 22 months late for fiscal years 2004 to 2007. HUD issued management decision letters, dated February 2 and April 13, 2009, to the City, along with required corrective

[4] Some findings and concerns were repeated.

actions for its fiscal years 2006 and 2007 audits, respectively. The letters detailed 8 findings, 16 material weaknesses, and 14 significant deficiencies identified in the City's single audit independent auditor's reports. As with HUD's monitoring review findings, these audits had not been cleared. For example, the City's fiscal years 2006 and 2007 audits reported deficiencies in its computer access controls, including not removing terminated/transferred employees and formal security policies, procedures and standards not being updated by management. During the review, we noted that the City still had not formally adopted its updated security policies and had not removed from the City's computer system a terminated housing department employee and three transferred employees.

More than two years after being notified via monitoring review letters, the City had failed to sufficiently address HUD's concerns. The city manager said that he believed the City's troubles with HUD were attributable to a different interpretation of requirements and communication issues. Because HUD continued to approve the City's action plans, he thought issues were being addressed. It is ultimately management's obligation to ensure that the City meets its fiduciary responsibilities and is responsive to HUD's concerns. HUD should require that the City provide timely and satisfactory responses to its correspondence and hold the City accountable for providing inadequate and/or incomplete responses or its failure to respond.

*The City Could Not Support the Accuracy of Its Data Used to Monitor Foreclosures*

Data the City used to monitor monthly foreclosures in the seven zip codes that it chose to serve under NSP was inaccurate. For NSP, HUD required the City to describe how its program would impact areas of greatest need, including those with the greatest percentage of home foreclosures, with the highest percentage of homes financed by a subprime mortgage-related loan, and identified by the City as likely to face a significant rise in the rate of home foreclosures. The City chose zip code boundaries as its method to select areas where the highest number and concentration of foreclosures occurred during a one-year period. The City monitored the seven zip codes to ensure that it continued to meet its greatest need requirements.

The City provided seven months of detailed data[5] that it used to monitor ongoing foreclosure activity in the identified seven zip codes. Testing of data for two of the seven months revealed errors. For example, the City failed to exclude foreclosed properties that should not have been included, such as vacant land or properties that were still occupied. Also, the City combined zip code foreclosures when reporting the total foreclosure amount, causing an appearance of more foreclosures. The City did not review the data it obtained to verify whether the data were accurate. Consequently, the City could not assure itself or HUD that its use of NSP funds would continually be targeted to the areas of greatest need. HUD should require the City to effectively monitor its program to ensure that it meets its greatest need requirements.

*The City Did Not Follow Its Procurement Policies*

The City did not follow its procurement policies for contracts similar to those it will enter into for its HERA and ARRA programs. Review of 15 City contracts from a variety of programs concluded that the City's contracts did not contain required contract causes and lacked

[5] October 2008 through April 2009

documentation for decisions made and that the City lacked a contract log for one of its programs. Also, three contractors received more than 81 percent of the Area Lead Education Reduction Training Program (ALERT) rotational contracts. Further, subcontractors did not comply with City requirements, and the City lacked specific policies regarding subcontractor responsibilities and approval authority.

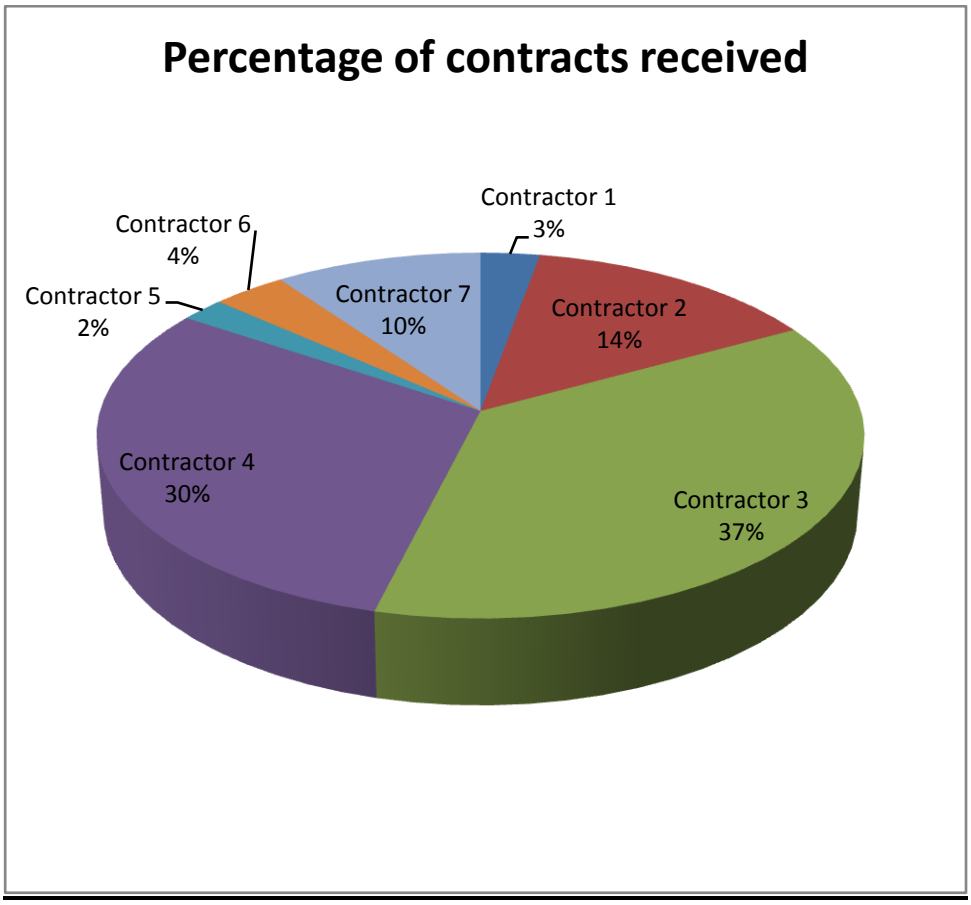
The City did not include the following contract clauses required by HUD regulations:

| Emergency shelter grant contracts | Home improvement program contracts | Area lead education reduction training program contracts |
|---|---|---|
| • Administrative remedies for breach | • Administrative remedies for breach<br>• Termination for cause<br>• Equal employment opportunity provisions<br>• Anti-Kickback Act<br>• Davis-Bacon Act<br>• Contract work hours and safety standards act<br>• Access and records retention<br>• Mandatory standards and policies on energy efficiency | • Anti-Kickback clauses<br>• Contract work hours and safety standards<br>• Davis-Bacon Act (not originally required but currently required by HUD for ARRA projects) |

Standard change order forms contained language stating that the change order was due to unforeseen circumstances but contained no specific explanation of the circumstances. Also, when the work exceeded the City's estimate, there was no documentation as to why the City accepted the price or whether it considered the validity of the price.

The City did not keep a contract log for all of its ALERT contracts, and in some instances, the emergency repair contract files only contained invoices and not contracts. In addition, for the home improvement program contracts, the City did not document the reason for change orders. The City must ensure that its contracts comply with HUD requirements and maintain sufficient support for contract decisions.

Contrary to the expectation, three of seven contractors received more than 81 percent of the ALERT contracts. According to a City program manager, the contractors for the ALERT contracts were to receive contracts on a rotational basis. The City could not provide an explanation as to why this situation occurred.




Subcontractors did not always follow City contract requirements. The City required subcontractors to expend funds in accordance with its contract and prohibited increasing or decreasing line-item amounts without the City's prior written approval. However, one subcontractor agreed to only charge the City 30.5 percent of its water bill but, instead, charged the City 90 percent. The subcontractor's explanation for the misallocation was that it was running out of funds on another grant. Contracting officers said that they were not aware of any City policy that detailed cost allocation requirements for the subcontracts. Their main concern was ensuring that actual expenses did not exceed budgeted amounts. However, to manage contracts properly, the City needs to ensure that expected accomplishments will not decrease as a result of these increased costs.

Further, the City did not have a specific policy regarding approval authority for purchases of goods and services. The City's request forms contained the following language: "Director's signature is only required on purchases greater than $8,500 and all HFC [*sic*] expenses." While the request forms required the approval of several officials, the forms lacked consistency regarding who was to sign. Most forms contained only one or two signatures; however, no forms reviewed that exceeded $8,500 contained the director's signature. The City's current director said that the former director required it, but he was not aware of any written policy covering the matter. The City's procurement and financial policies did not address signature requirements. The City needs to ensure consistency between policies and forms.

*Planned Sidewalk Improvements Did Not Meet the Purpose of Modernizing the Nation's Infrastructure*

The City planned to use its CDBG-R funds to provide sidewalk infrastructure in eligible census tracts/block groups. Of the four streets reviewed, only one appeared to meet the purpose of modernizing the nation's infrastructure in a responsible, prudent manner. The one street had 17 houses fronting it, and the street ran perpendicular to a main street. The other streets reviewed did not appear to be a prudent use of funds because of existing usable sidewalks or a significant number of vacant lots. In one instance, the City selected a side street which did not seem to have a practical purpose such as flowing to a school, and streets with houses fronting them were not selected. Further, City officials gave conflicting explanations about how they selected the sites. Managers explained that the City relied on a study of traffic flow patterns to determine the selections. Conversely, a City planner stated that the sidewalks chosen were not evaluated under a sidewalk study but ones not selected for reconstruction in the City's 2008 bond program. This City planner explained that his department did not develop a prioritized, comprehensive citywide list of sidewalks when the City asked. The City agreed to reconsider some of the proposed sidewalks and use the $17,920 on more prudent projects.

*Conclusion*

HUD placed special conditions on the City's $6.3 million NSP funding due to its history of unsatisfactory performance in administering its programs. The City will receive more than $4.5 million in HPRP and CDBG-R funding for additional programs. It is also planning to apply for more than $6 million in Lead-Based Paint Hazard Control Grant funding. Given the City's past performance, this substantial influx of additional funding may prove difficult for it to administer. The programs that the City plans to undertake will rely on management's ability to effectively manage the resources entrusted to it and to keenly discern the City's needs. The City must continue to work with HUD to correct the past deficiencies noted in HUD's monitoring reviews and audit reports. It must improve its procurement practices, including implementing consistent policies and oversight. HUD should continue its close monitoring of the City, including placing conditions on the City's HPRP and CDBG-R grants similar to those placed on the City's NSP grant.

## RECOMMENDATIONS

We recommend that the Director, Fort Worth Office of Community Planning and Development

1A. Place special conditions on the City's HPRP and CDBG-R grants similar to those placed on the City's NSP grant requiring the correction of past deficiencies and plans to monitor the additional funding, thereby ensuring better use of more than $4.5 million.
1B. Require the City to correct longstanding HUD and audit findings and timely submit audited financial statements.
1C. Require the City to implement and follow procurement policies and procedures including maintaining an accurate contract log. Establish and implement procedures to monitor subcontractors.

1D. Require the City to verify that it will serve the greatest needs with these funds.

1E. Require the City to use CDBG-R funds only on prudent projects. By doing so, the City has already saved $17,920 in funds not used for imprudent projects.

# APPENDIXES

## Appendix A

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

| Recommendation number | Unreasonable or unnecessary 1/ | Funds to be put to better use 2/ |
|---|---|---|
| 1A | | $4,543,341 |
| 1E | $17,920 | |

1/ Unreasonable/unnecessary costs are those costs not generally recognized as ordinary, prudent, relevant, and/or necessary within established practices. Unreasonable costs exceed the costs that would be incurred by a prudent person in conducting a competitive business.

2/ 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, the amount represents the amount of ARRA funds that will be better used by implementing the recommendations in this report.

## Appendix B

# AUDITEE COMMENTS AND OIG'S EVALUATION

**Ref to OIG Evaluation** **Auditee Comments**

August 11, 2009

Mr. Gerald R. Kirkland
Regional Inspector General
U.S. Department of Housing and Urban Development
Office of Inspector General, Region VI
819 Taylor Street, Suite 13A09
Fort Worth, Texas 76102

SUBJECT: City of Fort Worth, Texas, Needs to Strengthen its Capacity to Adequately Administer Recovery Funding

Dear Mr. Kirkland:

This letter is in response to your draft memorandum dated July 28, 2009 regarding your office's review of the City of Fort Worth's operations to evaluate the capacity of the City to administer the funding received through HERA and the American Recovery and Reinvestment Act of 2009 (ARRA). Enclosed please find responses to your findings and information on corrective actions taken to address concerns outlined in your review. The City of Fort Worth appreciates the professionalism exhibited by your staff and commends them for the orderly manner in which they conducted their review.

*The City Had a History of Failing to Meet Regulatory Requirements:*

**Comment 1**

The City acknowledges the existence of outstanding issues and previous deficiencies found by HUD in the administration of its grant-funded programs as well as former issues related to the timeliness of its annual audited financial statements. Over the past 2 years, and particularly in the most recent 12-month period, great strides have been made in correcting the deficiencies in these areas. Significant accomplishments have included completion of three Comprehensive Annual Financial Reports in a period of approximately 18 months, which has allowed the City to become current with its audit requirements. This enormous task involved the complete overhaul of the City's Financial Management Services Department and a huge increase in resources invested by the City to ensure fully compliant financial management and record-keeping for all funds, including federal grant funds. Additionally, the City has moved forward with clearing several of the findings outlined by HUD in past monitoring visits, has made repayment of a total of $558,698.41 for ineligible costs, and continues to work with the local HUD office to clear all remaining outstanding issues. The City has demonstrated in recent months its commitment to address all concerns completely and in a timely fashion, through the dedication and focus of senior management, ongoing changes in program management and constant communication with local HUD staff. Responsiveness to HUD concerns and compliance with HUD regulations are top priorities for the newly reorganized

**Comment 2**

*The City Could Not Support the Accuracy of Its Data Used to Support Its NSP Substantial Amendment*

The City acknowledges that there were inaccuracies in the raw data reviewed during the monitoring visit. It should be noted that the data report provided to auditors was an internal management tool put in place to monitor and evaluate monthly foreclosures on Fort Worth residential properties in order for program management to assure itself that the use of NSP funds continually targets the areas of greatest need as designated in the City's substantial amendment to its Consolidated Plan. The seven months of foreclosure activity provided to the OIG have been re-analyzed for accuracy. The results further validate that target zip codes in the substantial amendment are those continuing to experience the highest impact from single family residential foreclosures. The results of the re-analysis are provided in the chart below. Moving forward, the data will be reviewed to insure accuracy and used to monitor the extent of ongoing foreclosure occurrences. As seen below, the target areas actually represent a greater concentration of all foreclosure activity in Fort Worth following analysis of the corrected data, thereby confirming the city's original conclusion from its substantial amendment submission.

| **Single-Family Residential Foreclosures October 2008 through May 2009** | **7 months Original** | **7 months Corrected** | **Variance** |
|---|---|---|---|
| # Residential Foreclosures in Fort Worth | 6,025 | 5,756 | - 269 |
| # Foreclosures in Target Zip Codes | 2,723 | 2,726 | + 3 |
| Target area foreclosures as % of all Fort Worth SF residential foreclosures | 45% | 47% | + 2% |

**Comment 3**

*The City Did Not Follow Its Procurement Policies*

The City acknowledges that contracts did not contain certain required contract clauses and that there have been inconsistencies in the documentation used to track decisions made on certain projects. The City has moved to include the required clauses outlined by the OIG in all contracts going forward. Additionally, the City has moved to address the documentation and procedural concerns outlined by the OIG related to contractors and procurement. The Housing & Economic Development Department along with the Financial Management Services Department are working to review existing practices and make changes as needed to address the outlined concerns.

**Comment 4**

*Planned Sidewalk Improvements Did Not Meet the Purpose of Modernizing the Nation's Infrastructure*

The City is reviewing the overall list of sidewalks proposed to be addressed by CDBG-R funding to ensure that the improvements to be undertaken will meet all of the requirements of the CDBG-R funding The City will provide further detailed clarification on local procedures for ranking and prioritization of Capital Improvement Projects, which will demonstrate that selection of the designated locations meets all applicable regulatory requirements and the full intent of the ARRA statute.

**Comment 5**

*Conclusion*

Although the City of Fort Worth understands the basis for conclusions reached by the Office of Inspector General, demonstrated actions such as the full reorganization of both the Financial Management Services and Housing and Economic Development Departments, rapid repayment of identified ineligible costs, and consistent increased communication with HUD staff indicate that great strides are being made in addressing the issues outlined in the OIG memorandum. City staff continues to work diligently with local HUD staff to move forward in addressing the outstanding issues found in your report and in past HUD monitoring visits. The complete change in management in both the City's Financial Management Services and Housing & Economic Development Departments is but one clear sign that the City is serious in addressing these concerns. Consequently, based on the changes made by the City and the improvements already in place, the requirements outlined in the OIG recommendations are already being addressed and/or have been addressed. The City is confident that the changes and improvements outlined above along with the recent closing of most of the single audit findings, if taken into consideration, will increase optimism and confidence on the part of HUD officials in the City's ability to rectify all outstanding issues and successfully administer federal Recovery Act funding.

The City of Fort Worth appreciates the time and professionalism of your staff. We look forward to receiving your final report so that we may move forward implementing our various federally funded programs. If you have any questions, please contact Jesus Chapa, Housing & Economic Development Director, at (817) 392-5804 or jesus.chapa@fortworthgov.org.

Thank you.

Jesus (Jay) Chapa
Director, Housing and Economic Development Department

cc: Tom Higgins, Assistant City Manager

## OIG Evaluation of Auditee Comments

**Comment 1** We acknowledge recent strides the City has made to address HUD concerns and compliance with regulations. We reported on the evidence reviewed and analyzed during our capacity review.

**Comment 2** We modified this section of our memorandum. We appreciate the City implementing the recommendation.

**Comment 3** We appreciate that the City is taking steps to implement the recommendation.

**Comment 4** We appreciate that the City is taking steps to implement the recommendation.

**Comment 5** We acknowledge recent strides the City has made to address issues addressed in the memorandum. We appreciate that the City is taking steps to implement the recommendations.