

City of Moore

**Internal Audit Report on Design and Operating
Effectiveness of Internal Controls over CDBG-
DR Transactions**

July 2016

I. Executive Overview

Introduction

We recently completed a review of functions outlined below with a primary objective of evaluating the process and significant control points for effectiveness, adequacy, and efficiency of operations for the CDBG-DR processes performed by City of Moore (the "City"). The audit was conducted in accordance with the terms of our engagement letter and applicable internal audit guidelines. This report is intended solely for the information and use of management and the City Council, and should not be used for any other purpose. The City's oversight authorities may be provided with a copy of this report in connection with fulfilling their respective responsibilities.

It is important to note, we recognize the City of Moore's responsiveness to issues reported through the internal audit process. The City has appropriately allocated resources, attention, and brought on new staff to resolve these issues which have led to improvement in compliance practices. Furthermore, the City has demonstrated diligence in working to resolve high-risk issues by conducting proactive communication with the HUD Field Office to seek direct guidance as well as request technical assistance.

Audit Scope

We completed an audit of several functions of the City's CDBG-DR program in accordance with the terms of our engagement letter. The audit period covered January 1, 2016 through March 31, 2016. The functions covered in our audit for this period are outlined, as follows:

- Program policies and procedures
- Financial internal controls
- Eligibility of cost and procurement method

Our procedures were performed to:

- Evaluate the adequacy of internal controls in place to mitigate the identified risks,
- Evaluate the allowability of transactions,
- Evaluate newly developed policies and procedures as well as changes to policies and procedures following the April 2016 audit.

To accomplish this, we performed the following:

- Reviewed the following documents:
 - Procurement file for King's Manor Project
 - May 19, 2016 letter to HUD Field Office
 - Section 3 vendor training materials
 - City of Moore CDBG-DR Policies and Procedures: Infrastructure and Public Facilities
 - All active Housing Rehab Program files
 - H-02-W-LMI Environmental Review File
 - H-03-W-URG Environmental Review File
 - H-04-W-LMI Environmental Review File
 - City of Moore Section 3 Plan, July 20, 2015
 - Financial documentation for 1Q2016 expenditures
 - Draft Accounting Policies and Procedures Manual
 - Draft Section 3 Policy Guidance
 - DPA Program Authorization Update
 - ARCGIS census block group map for Cleveland County, OK
 - Moore Janeway Project Stakeholder Notes
 - DPA Market Analysis
 - PAC Meeting Minutes dated 02.23.2016
 - PAC Meeting Minutes dated 09.02.2015
 - SW-17 Janeway Master Plan
 - Redevelopment Visioning Meeting Posting Notices for 2016
- Interviewed key personnel in each function's area
- Reviewed all payroll as well as a random sample of CDBG-DR transactions up to March 31, 2016.

It should be recognized that controls are designed to provide reasonable, but not absolute, assurance that errors and irregularities will not occur, and that procedures are performed in accordance with management's intentions. There are inherent limitations that should be recognized in considering the potential effectiveness of any system of controls. In the performance of most control procedures, errors can result from misunderstanding of instructions, mistakes in judgment, carelessness, or other personal factors. Control procedures can be circumvented intentionally by management with respect to the execution and recording of transactions, or with respect to the estimates and judgments required in the processing of data.

Further, the projection of any evaluation of control to future periods is subject to the risk that the procedures may become inadequate because of changes in conditions, and that the degree of compliance with procedures may deteriorate.

Overview of Issues

During the course of our work, we discussed our findings with management. Our detailed findings and recommendations for improving controls and operations are described in the detailed issue matrix in Section I of this report. A separate listing of general enhancement opportunities not considered to be findings is described in section II of this report.

A summary of key issues is provided below along with the following information:

- Relative Risk is an evaluation of the severity of the concern and the potential impact on the operations. Items rated as "High" are considered to be of immediate concern and could cause significant operational issues if not addressed in a timely manner. Items rated as "Moderate" may also cause operational issues and do not require immediate attention, but should be addressed as soon as possible. Items rated as "Low" could escalate into operational issues, but can be addressed through the normal course of conducting business.
- Resolution Level of Difficulty is an evaluation of the estimated level of difficulty and potential cost to resolve the concern based on our experience. Items rated as "High" are considered to be difficult to resolve and/or will require a significant amount of planning and management involvement/oversight in order to obtain resolution. Items rated as "Moderate" are not as difficult to resolve and/or do not require a significant amount of planning, but may be time-consuming to resolve. Items rated as "Low" are items that are not complex and/or do not require significant amounts of planning and time to resolve.

Summary of Results			
Issue Description	Page	Relative Risk	Resolution Level of Difficulty
2016-07-01 *Unauthorized Down Payment Assistance Program	6	High	Moderate
2016-07-02 *Noncompliance with Section 3 program requirements	7	High	High
2016-07-03 *Noncompliance with CDBG-DR income requirements	8	High	Moderate
2016-07-04 *Discrepancies between General Ledger and Project Ledger	9	Moderate	Low
<i>*Indicates items of concern identified in previous audit reports that have not yet been brought to resolution.</i>			

Opportunities for enhancement are described in Section II of this report.

Conclusion

Audit ratings, as defined below, were assigned based on the identification of the key findings summarized above, as well as other less significant comments that can be addressed by management in the normal course of business.

Ratings	Conditions
Satisfactory	No significant issues noted. Controls are considered adequate and findings, if any, are not significant to the overall unit.
Needs Improvement	Some improvement is needed to bring the function to satisfactory status. If the deficiency continues without attention, it could lead to further deterioration and an unsatisfactory status.
Unsatisfactory	Significant deficiencies exist which could lead to financial loss or embarrassment to the City.

The following is a summary of the assigned rating for each function:

Ratings	Conditions
Internal Controls –Design Effectiveness	Needs Improvement
Program Design	Unsatisfactory
Internal Controls – Operating Effectiveness	Needs Improvement

I. Observations and Recommendations

Internal Controls – Design Effectiveness

Observation	Recommendation
1. The Down Payment Assistance Program has not been authorized by HUD. We observed the City's Down Payment Assistance Program has not been authorized by HUD through the existing Action Plan and Action Plan Amendment 1.	<p>We recommend the City obtain HUD approval through the submission of a second Action Plan Amendment to appropriate funds and authorize activity on the newly developed Down Payment Assistance Program. Any funds expended on this activity are at risk of recoupment without prior HUD authorization.</p> <p>The City has demonstrated that it is in contact with its local HUD field office regarding this issue. We recommend continued follow up, and escalation to the nation office if a response is not rapidly forthcoming.</p>
Management Response: The City is aware the DPA is not included within the approved Action Plan. The City has developed policy and procedures for a DPA program. The City is working with the U.S. Department of Housing and Urban, Community Planning and Development, Office of Block Grant Assistance, Disaster Recovery and Special Issues Division. The City has made proper notification and Division Director Tennille Smith Parker is aware of the issue. Director Parker and her team are working with the City to resolve the issue related to meeting the overall be LMI concern. The City is waiting on the resolution and guidance from HUD to move this program forward. Date of last communication on this issue was July 20, 2016.	

Program Design

Observation	Recommendation
<p>2. Noncompliance with Section 3 program requirements.</p> <p>We observed the following deficiencies in the Section 3 program:</p> <ul style="list-style-type: none">• Noncompliance with Section 3 training goal• Noncompliance with Section 3 employment goal• No evidence of outreach and recruitment efforts• No documentation of impediments to meeting Section 3 goals from contractors• Lack of compliance monitoring plan and implementation	<p>We recommend the City overhaul its Section 3 program design and implementation. Noncompliance with HUD's regulations in 24 CFR Part 135 may result in sanctions, termination of the Recipient's contract for default, and debarment or suspension from future HUD assisted contracts. (24CFR135.38(F)).</p>
<p>Management Response:</p> <p>To address noncompliance with Section 3 program requirements the City of Moore redesigned the Section 3 Plan including implementation and monitoring efforts. The draft Section 3 Plan is distributed to all primary construction contractors. The Plan will be on City Council's Agenda for August 15, 2016.</p> <ul style="list-style-type: none">• To minimize noncompliance with Section 3 training goal the contractors or subcontractors either provides directly, contracts with a third party, or requires completion of an existing training or training program targeted at increasing the Section 3 residents' capacity or skills to be employed by the contractor/subcontractor. To meet these criteria, the contractor/subcontractor will maintain in their Section 3 file:• A Section 3 New Employee Form (VDR-05B) for each potential new employee who attended the training; and• A course outline and a sign-in sheet for internally conducted or contracted training; or• A course certificate, license or other form of certification for a required training or training program; and• Any statements regarding impediments encountered despite actions taken.• To minimized noncompliance with Section 3 employment goal revision is reflected in the Section 3 Plan: V. Numerical Goals for Section 3 Residents and Section 3 Business Concerns heading. Contractors and subcontractors may demonstrate compliance with the "greatest extent feasible" requirement of Section 3 by meeting the numerical goals set forth herein for providing training or employment to Section 3 Residents and/or contracting opportunities to Section 3 Business Concerns. The goals are: 30% of new hires are Section 3 residents of the City of Moore and 10% of the contractors or subcontractors meet the definition of a Section 3 Business Concern. The numerical goals are not set-asides or quotas but instead establish a "safe harbor" for contractors and subcontractors on the matter of compliance with Section 3. In the absence of	

evidence to the contrary, a contractor/subcontractor that meets the minimum numerical goals for all new hires and contracting opportunities will be considered to have met the Section 3 requirements.

- Risk analysis determines a contractor's experience with HUD funding requirements, specifically compliance with Section 3 and Davis Bacon requirements experience. This process assists in creating the monitoring plan. Implementation of monitoring plan's effectiveness will be evidence in the compliance evaluation, which includes proof of outreach/recruitment efforts, impediments to meeting Section 3 goals. In evaluating compliance under the City's Section 3 Plan, a contractor or subcontractor that has not met the numerical goals described above has the burden of demonstrating why it was not feasible to meet the numerical goals identified in the City's Section 3 Plan. Such justification may include statements regarding impediments encountered despite actions taken. The contractor or subcontractor should refer to Attachment H of the Section 3 Plan for a list of acceptable methods that when documented, demonstrate compliance with Section 3.

Efforts to employ Section 3 residents should, to the greatest extent feasible, be made at all job levels (entry level and skilled positions) for those residents who are qualified (i.e., persons who are able to successfully complete the work required of the position). The following are descriptions of each form of Section 3 activity; the applicable criteria which if met would constitute a safe harbor; and the documentation necessary to support the Section 3 activity: A New Employee Form (VDR-05B) for each new hire made by the contractor; A New Hire Weekly Summary (VDR 05-C) for each week of the contract; A New Employee Form (VDR-05B) for each new hire made by the subcontractor who will receive more than \$100,000 in Federal funds; and Any statements regarding impediments encountered despite actions taken. To meet these criteria, the contractor/subcontractor will maintain in their Section 3 file.

Internal Controls – Operating Effectiveness

Observation	Recommendation
3. Current projects do not demonstrate compliance with HUD National Objective regarding income requirements. We observed the majority of the City's infrastructure and housing projects both in development and underway serve a population in census tracts with a low-to-moderate income (LMI) percentage below 50%.	The City has demonstrated that it is in contact with its local HUD field office regarding this issue. We recommend continued follow up, and escalation to the nation office if a response is not rapidly forthcoming. While the City's circumstances regarding the geographical location of the applicable event's impact relative to the City's documented, concentrated low-to moderate-income population areas, LMI compliance remains a significant risk until HUD grants a waiver ratifying the City's approach.
Management Response: The City is working with the U.S. Department of Housing and Urban, Community Planning and Development, Office of Block Grant Assistance, Disaster Recovery and Special Issues Division. The City has made proper notification and Division Director Tennille Smith Parker is aware of the issue. Director Parker and her team are working with the City to resolve the issue related to meeting the overall be LMI concern. Date of last communication on this issue was July 20, 2016.	

Observation	Recommendation
<p>4. We observed a discrepancy between the General Ledger and Project Ledger</p> <p>We observed a discrepancy approximately in the amount of \$60,000 (including \$40,000 from prior audit observation and \$20,000 of payroll adjustments waiting to be made on the GL from the outsourced CPA) between the City wide General Ledger and the Grant Project Ledger.</p>	<p>This discrepancy appears to be due to untimeliness of the General and Project ledger reconciliation. Another issue is the city converting to new software (MUNIS) while payroll is done in the old software (INCODE). This causes the benefit deductions to be hard-keyed by program staff on a monthly reconciliation and given to the external CPA to make entry adjustments. Program staff identified that the adjustments would be addressed by the end of next month and would reflect in the system.</p> <p>As a best practice, this reconciliation should be performed on a quarterly basis at a minimum.</p>
<p>Management Response:</p> <p>Reconciliations of the Project Ledger to the General Ledger are being performed on a monthly basis. Two areas of concern have been identified. The journal entries to remove payroll not pertaining to the disaster grant need to be performed in a timely manner, and the data from Incode software to Munis software did not convert properly. Support for these entries will be provided to the CPA making the adjustments on a monthly basis by the Accountant II. The Assistant Finance Director will perform manual entries to correct the data that converted incorrectly.</p>	

II. Enhancements

Observation	Recommendation
1. City website was not up-to-date with community engagement documentation as program staff intended.	The City's recent community engagement activities regarding the Redevelopment project was intended by program staff to be documented on the public-facing portion of the City's website. This documentation was not available on the City's website.
Management Response: The City posts all community engagement items on the website months in advance and have it promoted leading up to the event/meeting etc. Once the event is completed the City removes it from the website. The City will amend the way website items are posted by ensuring an archived section is created within the webpages pertaining to federal programs. This will make all community engagement items visible to the public pre and post the event.	We recommend that documentation of public engagement activities be made available on the City's website and that program staff monitor the website on a regular basis to ensure that material intended to be available to the public is present and accessible.