



City of Dunkirk

Community Development Block Grant Management

Report of Examination

Period Covered:

April 1, 2008 — June 13, 2012

2012M-146



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Table of Contents

	Page
AUTHORITY LETTER	2
INTRODUCTION	3
Background	3
Objective	4
Scope and Methodology	4
Comments of City Officials and Corrective Action	4
COMMUNITY DEVELOPMENT BLOCK GRANTS	5
Monitoring by City Officials	6
Sub-Recipient’s Use of CDBG Funds	7
Real Property Acquisitions	11
Loan Program	12
Grants to Local Businesses	14
Recommendations	17
APPENDIX A Response From City Officials	18
APPENDIX B Audit Methodology and Standards	20
APPENDIX C How to Obtain Additional Copies of the Report	22
APPENDIX D Local Regional Office Listing	23

State of New York Office of the State Comptroller

Division of Local Government and School Accountability

November 2012

Dear City Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for tax dollars spent to support government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Common Council governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit of the City of Dunkirk, entitled Community Development Block Grant Management. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the General Municipal Law.

This audit's results and recommendations are resources for local government officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

*Office of the State Comptroller
Division of Local Government
and School Accountability*

Introduction

Background

The City of Dunkirk (City) is located in Chautauqua County and has a population of approximately 12,600 residents. The City is governed by its Charter and other laws of the State of New York. The Common Council (Council), consisting of five elected members, has overall responsibility for the City's operations and can adopt and amend local laws, ordinances, and resolutions. The Mayor is the chief executive officer of the City and is responsible for the proper administration of City affairs. The Mayor appoints various department heads and other administrative staff to assist with supervising and managing the City's daily operations.

The Community Development Block Grant (CDBG) program provides funding to revitalize neighborhoods, expand affordable housing and economic development, and improve community facilities and services. The U.S. Department of Housing and Urban Development (HUD) oversees the CDBG program and allocates grants directly to eligible communities.

The City's Director of Development and the CDBG Coordinator are responsible for managing and overseeing the use of these funds. The City is awarded CDBG moneys pursuant to annual funding agreements with HUD. For the four-year¹ period ending March 31, 2012, the City has received over \$2 million in CDBG grant funding. The Dunkirk Local Development Corporation (DLDC)² acts as a sub-recipient of the City's CDBG program funds. According to the funding agreements, the Council intended to pass CDBG moneys to the DLDC to fund a revolving loan program and provide financial assistance to eligible businesses through loans and grants.

¹ The grant program fiscal year is April 1 through March 31.

² Although the DLDC is a separate and distinct entity managed by a Board of Directors (Board), the DLDC does not have its own employees. The DLDC's by-laws provide that certain City officials – by virtue of their positions – hold certain DLDC positions and that the authority to appoint other members or directors of the DLDC rests primarily with the Mayor. City officials, including the City's Director of Development and the CDBG Coordinator, perform the DLDC's day-to-day operations without additional compensation from the DLDC. Therefore, it appears that City officials who also held DLDC positions did not act as though they were working for two separate entities. As such, we found that City officials often managed the finances of the two entities as if they were one entity. For example, the DLDC disbursed moneys for City-managed CDBG projects, while the City disbursed CDBG funds on behalf of the DLDC for loans and agreements negotiated by the DLDC.

Objective

The objective of our audit was to evaluate the City's financial management and administration of the Community Development Block Grant program. Our audit addressed the following related question:

- Does the City properly account for and monitor the administration of the Community Development Block Grant program and the activities of the grant sub-recipient?

Scope and Methodology

We evaluated the City's grant accounting and administration monitoring for the period April 1, 2008, through June 13, 2012.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix B of this report.

Comments of City Officials and Corrective Action

The results of our audit and recommendations have been discussed with City officials and their comments, which appear in Appendix A, have been considered in preparing this report. City officials generally agreed with our recommendations and indicated that they already have taken, or will take, corrective action.

The Council has the responsibility to initiate corrective action. A written corrective action plan (CAP) that addresses the findings and recommendations in this report should be prepared and forwarded to our office within 90 days, pursuant to Section 35 of the General Municipal Law. For more information on preparing and filing your CAP, please refer to our brochure, *Responding to an OSC Audit Report*, which you received with the draft audit report. We encourage the Council to make this plan available for public review in the City Clerk's office.

Community Development Block Grants

The primary objective of the Community Development Block Grant program is to aid in the development of viable urban communities by providing persons of low and moderate income with decent housing, a suitable living environment, and expanded economic opportunities. Pursuant to CDBG program regulations, grant recipients are responsible for establishing priorities and developing funding plans. Federal regulations establish eligible activities and the national objectives that each activity must satisfy. Additionally, in developing its funding plan, a grant recipient must give priority to activities benefiting low and moderate income persons. The Council and Mayor have a shared responsibility to ensure grant activities are completed in a timely manner and in compliance with relevant laws and regulations. The Council may authorize contracting with a private individual, not-for-profit agency, or consulting firm, as a “sub-recipient,” to receive CDBG funds and effectuate certain activities on the City’s behalf. However, the ultimate responsibility for proper financial management of all CDBG funds rests with the Council and Mayor.

We found that City officials³ have severely mismanaged the CDBG program and have put significant public funds at risk. City officials have disbursed CDBG funds without the most basic of documentation to support the expenses and have used the funds at times to pay for a variety of miscellaneous expenses that have no connection to the CDBG program. Most disturbing is that some of these transactions have been recorded in a manner to apparently hide the true nature of the transactions.

City officials could not provide adequate documentation to support claims paid with CDBG funds or demonstrate how Federal program requirements were being met. We identified where City officials have disbursed more CDBG funds than was properly authorized, spent funds on items that are not eligible under the CDBG program, and spent over \$500,000 for no legitimate CDBG purpose. In addition, they have made nearly \$400,000 in loans that are unsecured and lack the most fundamental paperwork, such as a signed loan document. All told, we determined that more than \$1.1 million may have been wasted or misused to fund ineligible, questionable, and unauthorized

³ The current Mayor is newly elected and began his term on January 1, 2012. Prior to his initial term as Mayor, he served as a member of the City’s Common Council. For the majority of the audit period, the former Mayor was in office and was primarily responsible for overseeing the proper use of the CDBG funds we reviewed.

activities, as detailed in Table 1. We are referring our report to the U.S. Department of Housing and Urban Development (HUD) for further review.

Table 1: Ineligible, Questionable and Unauthorized Activities	
DLDC Chairman’s Travel	\$15,000
Bonus Payments to DLDC Chairman and DLDC Treasurer	\$6,600
Ineligible Equipment	\$41,000
Property Acquisitions	\$500,000
Unsupported Loans	\$396,000
Grants to Local Businesses	\$175,000
Total	\$1,133,600

Monitoring by City Officials

To receive its CDBG grant award, the City must develop and submit to HUD a comprehensive planning document and an application for funding called the annual action plan⁴ (Plans). In its Plans, the City identifies its community development goals and describes how CDBG grant funds will be used to satisfy these goals. The Plans also identify and describe in detail the development activities that the City intends to fund with CDBG moneys. The Department of Development presents the Plans to the community at multiple public hearings and then to the Council for approval. As such, the Plans serve as the basis for managing the CDBG program, ensuring compliance with Federal requirements, and monitoring the City’s progress toward achieving community development goals.

While it is essential for the Council and Mayor to monitor the CDBG program to ensure that community development goals are being met and moneys are used as intended, they failed to do so. Examples of the lack of monitoring by the Council and Mayor include the following:

- The Council approved the transfer of \$557,000 to the DLDC for the four-year period, but City officials⁵ transferred approximately \$715,000 directly to the DLDC and paid an

⁴ At the beginning of each five-year grant period, the City is required to submit a multi-year planning document, referred to as the Consolidated Action Plan, outlining the program’s overall goals. In addition to the multi-year planning document, the City must annually submit an action plan. This annual action plan is approved by the Council and describes in detail the manner in which the City intends to use CDBG funds for the grant year. Our use of the term “Plans” refers to the annual action plans during the audit period.

⁵ To obtain CDBG funds from the City, the DLDC Chairman, who was also the City’s Director of Development, would submit a draw-down request to the City Fiscal Affairs Office. The draw-down requests were approved by the City Treasurer. The disbursements were approved by various City officials, including the Director of Development, Mayor, Treasurer, and Fiscal Affairs Officer.

additional \$173,000 to various local businesses on behalf of the DLDC. As such, the DLDC had access to \$331,000 more in CDBG funds than was authorized by the Council.

- In June 2009, the City provided the DLDC with \$110,000 for the revolving loan program. The voucher and drawdown request had no supporting documentation attached and City officials were unable to identify the corresponding loans or provide us with any documentation to demonstrate what this money was intended to be used for.
- Periodic status and expense reports would allow City officials to identify and address any issues in a timely manner and keep the public informed on the progress of program activities. However, the Council did not establish a formal monitoring process and did not request periodic reports from the Department of Development or the DLDC.

This lack of oversight places grant funded projects at risk of mismanagement and compromises the transparency of the community development program.

Sub-Recipient's Use of CDBG Funds

Sub-recipients are entities provided with CDBG funds by a grant recipient to carry out agreed-upon activities that the grant recipient cannot or does not want to carry out itself. However, direct responsibility for completion of grant activities, compliance with relevant laws and regulations, and proper financial management of CDBG funds rests with the grant recipient.

Written Agreement — HUD regulations require that a written agreement between the grant recipient and sub-recipient be in place prior to CDBG funds being placed in the custody of a sub-recipient. Such an agreement is essential for defining the nature of activities to be carried out by the sub-recipient, the manner in which CDBG funds may be used by the sub-recipient, the timeframe for completing activities, and the records or reports the sub-recipient must submit to the grant recipient to demonstrate compliance. The City, as grant recipient, is responsible for executing a contract with the sub-recipient and monitoring the sub-recipient's use of grant funds.

The DLDC's primary source of revenue is CDBG grant moneys transferred from the City for a revolving loan program and other economic development projects. During the four-year grant period reviewed, City officials provided the DLDC with over \$888,000 in CDBG grant moneys to fund various economic development projects. The CDBG Coordinator provided us with copies of two sub-recipient agreements, for the 2009 and 2010 grant years, that were

never authorized⁶ by the Council. No agreements appear to have been executed for the 2008 and 2011 grant years. Furthermore, the two agreements that were provided were inadequate because they failed to fully describe the agreed-upon activities that the DLDC would perform on behalf of the City. Additionally, the funding plan in the two agreements differed significantly from the amount of CDBG funding approved by the Council.

In the absence of adequate agreements, City officials do not have an appropriate basis on which to adequately monitor the use of its CDBG grant funding by the DLDC. As a result, the City's CDBG grant funding is at risk of waste or misuse, and the Council and Mayor cannot properly monitor the progress of development activities to ensure projects are completed on time and within approved funding parameters.

Segregation of Duties — Despite the absence of Council-authorized written agreements, the DLDC has nonetheless acted as the sub-recipient of CDBG moneys. Therefore, City officials have a responsibility to ensure that there are effective controls in place to safeguard grant funds. This includes adequately segregating duties so that no one individual has control of all fiscal functions. For example, the same person should not authorize payments, prepare and issue checks, and update the accounting records. If segregation of duties is not possible, additional oversight should be provided as a compensating control.

The DLDC Chairman (i.e., the City Director of Development) performed the DLDC's day-to-day financial operations, which included authorizing expenses and signing checks without oversight. We reviewed the DLDC's bank statements and canceled check images for the period January 1, 2009, through April 30, 2012, and identified 109 payments totaling over \$27,000 that were issued to either the former⁷ DLDC Chairman (Chairman) or the DLDC Treasurer (i.e., the City CDBG Coordinator).

We reviewed the supporting documentation for these payments and found that the Chairman improperly used \$13,000 in CDBG funds to reimburse himself for unauthorized travel expenses and an additional \$2,000 to pay for unauthorized conference registration fees. This occurred because the Chairman authorized and approved all of his own travel expenses. Although his travel expense reimbursements were

⁶ Although the agreements were signed by the Mayor, Article IV of the City Charter assigns the power and authority to approve contracts to the Common Council.

⁷ The former Chairman (Director of Development) was appointed by the former Mayor in August of 2008 and served until the new Mayor took office in January 2012. We found no checks issued to the current Chairman (Director of Development).

supported by documentation such as hotel and flight confirmations and photocopied credit card receipts for meals, the Chairman did not document the purpose for his travel or how his travel would benefit the City or the DLDC. Furthermore, the DLDC Board did not approve his travel or the reimbursements.

The Chairman also paid himself a total of \$2,300 and the DLDC Treasurer a total of \$4,300. The DLDC Treasurer stated that these payments were monthly “bonus” payments to reimburse the two City officials for various activities related to the operation and management of the DLDC, including additional work they did to host community events. The payments were not supported by documentation and there was no evidence that the “bonus” payments were authorized by either the DLDC Board or the Council. As City officials, their annual salaries were approved by the Council at the time of their appointments. Without authorization from the Council or Board, the Chairman lacks the authority to use City CDBG funds to pay himself and the DLDC Treasurer.

In addition to these unauthorized payments, we found that the Chairman issued and cashed a check payable to “Cash” in the amount of \$75,042.48. The canceled check image showed that the check was signed and endorsed by the Chairman. Although the check was not documented in the DLDC Treasurer’s records,⁸ we were eventually able to determine that the \$75,042.48 was supported by a valid loan agreement. We also confirmed with the financial institution that the Chairman purchased a “bank check” in the same amount on the same date he cashed the check. There was no documentation why this transaction was orchestrated in this manner. The Chairman’s ability to initiate and execute this type of transaction with little or no oversight demonstrates the severity of the DLDC’s internal control weaknesses.

Because the Chairman is able to perform all of the cash disbursement functions without Board authority or oversight, there is a significant risk that grant money could be misused and disbursed for inappropriate purposes.

Ineligible Activities — All activities⁹ funded with CDBG moneys must satisfy one of the three national objectives: benefiting low and moderate income persons, preventing or eliminating slums or blight, and meeting urgent community needs. Federal regulations specifically

⁸ The DLDC Treasurer’s records did not identify the DLDC check written to cash. However, upon inquiry, the DLDC Treasurer provided us with a copy of the “bank check” purchased by the Chairman.

⁹ Except certain activities carried out under the eligibility categories of planning and capacity building, program administration, and technical assistance.

identify several activities as ineligible, such as general government operation expenses and political activities. Additionally, purchases of equipment and motor vehicles are generally considered ineligible activities. We found that City officials had improperly used over \$41,000 of CDBG moneys to purchase various pieces of equipment, as follows:

- In December 2010, City officials leased a dump truck for the Department of Public Works. The City used \$1,562 as a down payment on the vehicle and then made monthly lease payments of \$763 from February 2011 until May 2012. As of May 2012,¹⁰ payments for the ineligible truck totaled more than \$13,500.
- The City purchased two utility vehicles for the Parks Department for approximately \$11,500. In addition, the costs were allocated to the “streetscape project.” According to the Plans, this project is to improve community areas and street scenes or public facilities. It appears that officials recorded these payments in this manner to conceal the true nature of the transactions.
- In April 2009, City officials reimbursed the DLDC for outdoor cinema equipment it had purchased for approximately \$11,000. City officials could not demonstrate how the purchase of an outdoor cinema satisfied one of the CDBG program’s three national objectives. Further, City officials initially were unable to locate the equipment when we requested to see it. City officials eventually located the equipment in the possession of a third-party vendor, with whom it had been left since the prior summer.
- In July 2009, the City used \$5,000 to help pay for a used undercover police vehicle purchased for \$8,500. A police vehicle is not an eligible equipment expense. Further, the purchase was recorded by City officials in the financial records as “water treatment plant improvements,” apparently to conceal the true nature of the purchase.

Because the Council did not properly monitor CDBG program activities, payments were made for equipment purchases that were not eligible to receive CDBG funding.

¹⁰May 2012 was the last monthly payment made at the time of our review. This truck lease requires additional monthly payments through November 2013, aggregating to \$27,477 (principal and interest) for the entire lease term.

Real Property Acquisitions

For the acquisition of real property to qualify as an eligible CDBG activity, one of the national objectives must be met. We found that the City has spent over \$500,000 for two property acquisitions that City officials could not justify.¹¹

The most significant questionable property acquisition occurred in July 2010, when the City made the first in a series of reimbursements to the DLDC for the purchase of a former car dealership located on the waterfront. The DLDC purchased the property for \$525,000. However, the DLDC did not obtain an appraisal prior to the purchase, and the property was assessed with a full market value of \$361,000 in 2010. As of June 2012, \$300,000 has been paid toward the property's purchase price. The DLDC also has used \$29,000 of CDBG funds to demolish a structure¹² and an additional \$148,145 to pave and improve the parking lot, which brings the total amount of CDBG funds expended on this property to more than \$477,000. There is still more than \$225,000 plus interest outstanding for the remainder of this property's purchase price.

Officials could not demonstrate how this property furthered the goals of the CDBG program. Currently, the property appears to be used primarily as parking for patrons of a neighboring restaurant.

Further we are troubled by the excessive interest rate the City is paying on a mortgage for the property. The DLDC and the seller of the property entered into a mortgage agreement allowing the DLDC to finance part of the cost of the property over a five-year period at an escalating rate of interest. For the first year of the mortgage, the interest rate was 6.5 percent, which increases by 0.5 percent each year to 8.5 percent for the final year of monthly payments, ending in 2015. This arrangement results in total interest expense exceeding \$76,000. Based on the historically low interest rates which have been prevalent in recent years, especially for such a short-term loan, DLDC officials appear to be paying excessive interest costs. As a result, we question whether DLDC officials acted in the best interest of the City and the CDBG program when negotiating these terms. Moreover, officials could not demonstrate that they compared this financing option to other available financing to be sure they obtained the best financing source.

¹¹ As defined in HUD Regulations 24 CFR 570.209(b), public benefit would result from the creation or retention of jobs and/or providing goods or services to low and moderate income persons.

¹² Under the terms of the mortgage agreement, the building located on the property at the time of sale was not to be "removed, demolished, or altered" without the seller's consent. However, there was no documentation to indicate that City officials or DLDC officials obtained consent from the seller prior to demolishing the building.

The second questionable property acquisition occurred in October 2009; the DLDC bought a vacant building for \$50,000. No appraisal was obtained prior to the purchase, and the property was assessed with a full market value of approximately \$22,000 in 2009. As such, the DLDC cannot demonstrate that the acquisition price was reasonable. Further, the DLDC Board and City officials did not document the intended purpose for this property or how it met a national objective. The property remains vacant as of June 2012.

Based on the Plans, the Council did not intend to allocate CDBG funding to the DLDC for real property acquisitions. Furthermore, since the DLDC has not clearly documented an intended use for either property, it is not possible to determine whether the acquisitions will meet a national objective or be aligned with the City's community development goals.

Loan Program

The City also used CDBG moneys to fund a revolving loan program to assist local businesses. The City disbursed a total of \$427,500: \$103,800 to four local businesses under loan agreements negotiated by the DLDC and \$323,700 to the DLDC, which the DLDC used to fund loans to 10 local businesses. We reviewed the files and records for loans made to these 14 businesses and found that City and DLDC officials failed to maintain adequate documentation for loans totaling almost \$396,000. Because this is a revolving loan fund, if loans are not repaid, moneys are not available for other qualified businesses to further the City's economic development goals. Our exceptions with respect to these loans are as follows:

- In January 2010, the City transferred \$103,520 to the DLDC to reimburse it for a portion of loans the DLDC provided to a hotel.¹³ The DLDC made two payments of \$50,000 to the hotel, one in September 2009 and the other in December 2009. In addition, the DLDC paid a third party \$27,400 on behalf of the hotel in June 2009, for a total loan of \$127,400. A promissory note dated September 21, 2009, indicated that the DLDC would loan the hotel \$125,000 to be repaid over a 10-year period beginning February 1, 2010. It is unclear why the promissory note is for \$2,400 less than the amount actually loaned. A subsequent loan agreement, which apparently altered the terms of the promissory note, was dated January 6, 2010. This agreement indicated that the DLDC would loan the hotel \$175,000 to be repaid over a 20-year period beginning June 1, 2010. The agreement also includes a performance incentive forgiving \$50,000 of the loan if certain

¹³ This is the same hotel that received over \$76,000 in grants during the same four-year period, as discussed in the finding entitled Grants to Local Businesses.

hotel renovations and a proposed water park were completed by June 1, 2013. Although the loan amount was presumably increased to \$175,000, no payments have been made from either the DLDC or the City to the hotel beyond the \$127,400. As such, it is unclear what impact, if any, the \$50,000 incentive has on the revised terms of the loan. Moreover, the agreement states that at no time can the loan payments be more than 60 days delinquent. The hotel has not repaid any portion of the loan as of the end of our fieldwork. As of June 1, 2012, the hotel should have made loan payments totaling \$27,678.¹⁴ The current Director of Development was working with the City Attorney to address this.

- In September 2009, the DLDC Board adopted a resolution authorizing a loan of \$100,000 to a manufacturing company. Per the resolution, the loan would be forgiven if, after 36 months, the company has maintained a minimum employment level of 47 people in the City. However, the DLDC had no documents signed by the company agreeing to the terms authorized in the resolution. In September 2010, the City transferred \$110,000 of CDBG funds to the DLDC for the loan. The DLDC Chairman wired the company \$125,000, which was \$25,000 more than the amount authorized by the DLDC Board. Because no executed loan agreement or promissory note apparently exists, it is not clear whether the recipient is aware of its obligation to maintain the designated employment level and the extent to which the terms of the loan, as indicated in the DLDC Board minutes, are enforceable. As of the end of our fieldwork, City officials had not verified that the minimum employment level has been maintained and have not initiated any action to collect repayments from the loan recipient.
- In September 2011, the City disbursed \$34,300 in CDBG funds as a loan to a web design and brand marketing company. The loan terms, including the amount, repayment, and approved use, were negotiated by the DLDC. A loan commitment letter detailing the terms was signed by the DLDC Chairman and the company, but there was no promissory note or loan agreement on file. Furthermore, the loan commitment letter indicated that the loan principal and accrued interest would be forgiven if the company met “employment metrics.” However, no details regarding these metrics were included in the letter, so it is unclear how a determination will be made as to whether the company’s performance in regard to some employment

¹⁴ As of the June 1, 2012, due date, 25 monthly payments of \$1,107.14 should have been made.

statistic has been achieved to result in loan forgiveness. As of the end of our fieldwork, City officials have not initiated any action to collect repayments from the loan recipient.

Without records adequately documenting the terms and conditions of these loans, City officials have not protected the community's interest and cannot help ensure that community development goals will be accomplished or that loan repayments will be collected.

Grants to Local Businesses

In certain instances, CDBG moneys can be used to provide financial assistance or grants to private for-profit entities. For example, grants could be given to a local business for expansion to create jobs or as an incentive to retain jobs within the community. However, City officials have a responsibility to protect the public's interest whenever public funds, such as CDBG grant moneys, are used to benefit a private for-profit entity. To fulfill this responsibility, officials should perform a due diligence assessment of any financial assistance they provide to a for-profit business as a means of ensuring that public funds are not wasted and that the expected economic benefit from any project funded from CDBG moneys will meet a qualified national objective. Furthermore, any grants or funding should meet the City's own development goals as established by the Council in the Plans.

According to the Plans, the City would provide grants to local businesses through a "commercial façade program." Businesses could apply for a 50 percent matching grant up to a maximum of \$15,000 to improve the exterior appearance of their storefronts. Prior to receiving CDBG funds, grant recipients were required to submit proof of project completion and evidence of their 50 percent investment in the approved project. Although the façade program guidelines state that grant recipients would be selected by the City's Economic Development Committee,¹⁵ we found that all grant recipients were instead selected solely at the discretion of the former Director of Development.¹⁶ City officials could not demonstrate that grant recipients were solicited or selected using an open competitive process that would ensure all local businesses had an equal opportunity to apply and be considered for grants or that the selections were free from favoritism.

We reviewed grants of CDBG funds totaling more than \$223,000¹⁷ made to nine local businesses and question whether over \$175,000 in grants were an appropriate use of CDBG moneys, as follows:

¹⁵ This committee comprises three Common Council members.

¹⁶ The current Director of Development was appointed by the newly elected Mayor on January 1, 2012. The current Director had not approved any grants as of the end of our fieldwork.

¹⁷ See Appendix B, Audit Methodology and Standards, for details on our sample selection.

Hotel Improvements — From May 2010 through February 2011, City officials gave a hotel over \$76,000 for various improvements and renovations. The claims for payment were supported by estimates from third-party vendors and included \$15,000 as a commercial façade grant to construct an outdoor wooden pavilion in May 2010, \$18,500 for the purchase of a commercial laundry machine and \$12,500 to replace windows in January 2011, and \$30,000 for vinyl wall coverings and restroom renovations in February 2011. City officials could not demonstrate how these grants were in line with community development goals or satisfied one of the national objectives of the CDBG program. The construction of a pavilion does not qualify as a commercial façade project under the City’s façade improvement guidelines. Further, the hotel’s application was incomplete because it did not indicate the total cost of the project, and the hotel never submitted proof of actual expenses. In the absence of adequate documentation, we question whether these payments were eligible for the façade grant and/or an appropriate use of CDBG moneys.

Furthermore, \$30,000 of this amount was paid to the hotel from the City’s general fund. Although the general fund was reimbursed \$18,900 from CDBG moneys in May 2011, the remaining \$11,100 was never reimbursed to the City; as such, this represents a gift of public funds. The State Constitution prohibits municipalities from making gifts or loans to, or in aid of, private individuals or corporations.

DLDC Board Member’s Business — We found that the owner of a commercial flavoring business, who also served as a DLDC Board member at the time, received two commercial façade grants totaling \$22,500. The grants were for replacing the roof and windows and repairs to the factory foundation, all entrances, porches and steps. There was no application on file for either grant. As such, the project description and purpose was not properly documented, and it is unclear if all activities were eligible for reimbursement under the City’s façade program guidelines. The claims for payment were supported by vendor invoices that were not sufficiently detailed and were difficult to read because they were hand-written and illegible.

Restaurant Improvements — From May 2010 through August 2011, the DLDC paid more than \$32,000 to a restaurant for power-washing, painting, landscaping, a new sign, and paving and sealing the parking lot. The commercial façade grant program is a City-administered community development program, not a program managed by the DLDC. City officials were unable to explain why the DLDC made these particular grants on behalf of the City. However, when the City reimbursed the DLDC for the grants, City officials recorded approximately \$13,000 as expenses of the CDBG “streetscape

improvement program” instead of commercial façade grants. According to the Plans, funds allocated to the streetscape program were to be used to improve community areas, street scenes, and public facilities. It appears these payments were recorded as streetscape activities and paid through the DLDC to conceal the nature of the transactions or the amount paid to the restaurant. In the absence of adequate documentation, City officials could not demonstrate that these grants were an appropriate use of CDBG funds.

Food Manufacturer — In October 2011, the DLDC wired \$20,000 to a food manufacturing company and the City paid the company an additional \$20,000 in December 2011. The \$40,000 grant was supported by a letter dated July 1, 2009, indicating that the DLDC had awarded the company a \$50,000 grant to renovate and improve its shipping and receiving facility. However, the grant was never approved by the DLDC’s Board. Furthermore, City officials could not provide sufficient documentation to demonstrate how the grant satisfied the program goals and objectives or provided a public benefit. The DLDC could not provide us with documentation to indicate the responsibility or performance requirements of the grant recipient.

Flower Shop Addition — In May 2010, the City provided a commercial façade grant of \$4,632 for a flower shop addition. Although the store addition may be considered an appropriate economic development activity, the project did not qualify under the City’s façade improvement guidelines. The recipient’s application was incomplete and did not indicate the total cost of the project. Further, the recipient never submitted proof of actual expenses incurred. Instead, the claim for payment was supported by an estimate for various construction materials totaling \$4,632, the amount of the grant that was paid. However, façade grant recipients are only entitled to receive 50 percent of the total project cost. The documentation provided by City officials did not demonstrate how this project would satisfy national objectives or its own community development goals.

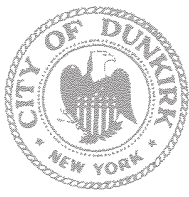
The Council did not fulfill its responsibility to oversee and ensure the appropriate use of CDBG funds. The Council did not monitor the City’s progress toward community development goals funded by the CDBG program or the manner in which City and DLDC officials used CDBG grant moneys. As a result, the City’s development grant funding has been at risk of waste or misuse, disallowed costs, and potential grant reductions from HUD. Further, if the City is required to reimburse the CDBG grant moneys that have been used improperly for ineligible activities, the City’s taxpayers could face a greater tax burden as a result of the City’s mismanagement of Federal grant moneys.

Recommendations

1. The Council should establish formal procedures to monitor the performance and administration of the CDBG program, including a review of periodic status reports on grant activity.
2. The Council should enter into a written agreement with the DLDC that clearly establishes the responsibilities of both parties including the work to be performed, a schedule for completion, and a budget. These documents should be in sufficient detail to allow the Council to monitor performance. Further, the agreement should specify the records the DLDC must maintain and the reports that must be submitted to the Council, including dates for submission.
3. The Council should authorize all transfers of CDBG funds to the DLDC only after ensuring they comply with the Council approved Plans. Funds should not be distributed in excess of the Council's express authorized limit.
4. The Council should ensure that the DLDC has effective control procedures in place to adequately safeguard grant moneys.
5. The Director of Development should inspect the DLDC's loan files to ensure adequate documentation is on file prior to providing the DLDC with grant funds for this purpose.
6. The Council and Mayor should require documentation sufficient to support all claims against the City's CDBG funds to demonstrate how moneys are being used to meet the program's objectives.
7. The Council should discuss with the City Attorney whether the City could require the DLDC to recover unauthorized payments made to the DLDC Chairman and DLDC Treasurer.
8. The Council and Mayor should establish formal procedures for selecting grant recipients through an open, competitive process that helps ensure all local businesses have an equal opportunity to apply and be considered for grants.
9. The Director of Development should ensure all façade grant projects and recipients comply with the City's program guidelines.

APPENDIX A
RESPONSE FROM CITY OFFICIALS

The City officials' response to this audit can be found on the following page.



CITY OF DUNKIRK
A Chadwick Bay Community

Office of the Mayor
City Hall, Dunkirk, New York 14048

ANTHONY J. DOLCE
MAYOR
(716) 366-9881
FAX (716) 366-2049

October 15, 2012

NYS Comptroller, Buffalo Regional Office
295 Main Street, Suite 1032
Buffalo, New York 14203-2510
Attn: Robert Meller, Chief Examiner

**Re: City of Dunkirk Report of Examination
Community Development Block Grant Management
2012M-146**

Dear Mr. Meller:

Please find this as the City of Dunkirk's written audit response to your office's above-referenced *Report of Examination*, presented to the City on October 1, 2012.

Certainly, we appreciate the time, attention and focus of your office as presented in the draft findings and recommendations. The City appreciates the guidance of your office as we work to address the short-comings outlined in the *Report*.

Details regarding corrective action and the implementation of practices and procedures geared to improve the City's overall internal over-sight and control of the Community Development Block Grant ("CDBG") program will be forthcoming in our Corrective Action Plan.

However, we are pleased to advise your office that even prior to receiving the draft *Report*, the City's Common Council on September 4, 2012 authorized the services of a specialist to assist the City and to provide technical and compliance assistance necessary for the administration of the City's CDBG program.

Should you have any questions, please do not hesitate to contact the undersigned at your convenience.

Thank you.

Sincerely,

Anthony J. Dolce, Mayor
City of Dunkirk

AJD/

CC: Hon. Common Council (five)

APPENDIX B

AUDIT METHODOLOGY AND STANDARDS

We examined the City's CDBG grant program for the period April 1, 2008, to June 13, 2012. To accomplish our audit objective and obtain valid audit evidence, our procedures included the following:

- We reviewed the City Charter and Administrative Code.
- We reviewed minutes of meetings of the Common Council and DLDC Board.
- We analyzed applicable CDBG program documents such as funding drawdown requests, annual action plans, and sub-recipient agreements. We also reviewed CDBG correspondence to and from HUD, such as the annual performance and evaluation reports, and letters or notices of compliance issues.
- To verify that CDBG funding is used for eligible activities and intended purposes, we compared CDBG funding disbursements to Federal regulations and the City's annual action plans. We also compared CDBG disbursements to the performance goals in the City's annual action plans to ensure that funded activities adequately satisfied the goals.
- We selected a biased judgmental sample of 75 CDBG disbursements totaling \$1.8 million by scanning payments recorded in the City's financial records and draw-down requests submitted to HUD. We selected large/material disbursements and/or large transfers of funds made to individuals or private businesses either in multiple amounts which totaled more than \$5,000 or single disbursements totaling more than \$5,000. We also scanned Council minutes and DLDC Board minutes, canceled checks, and bank statements to identify payments made to the DLDC during the audit period and identified 44 transfers totaling \$715,000 that were made from the City to the DLDC.
- We interviewed appropriate City and DLDC officials and personnel to determine how the Council monitored the CDBG program and the DLDC's activities.
- We reviewed agreements between the DLDC and loan recipients.
- We reviewed the following records as they related to the CDBG program:
 - o Policies and procedures (regulations)
 - o Various financial reports including budget status reports, revenue status reports, trial balances, account detail reports, and audited financial statements
 - o Claims and vouchers and supporting documentation for CDBG disbursements

- o Drawdown documentation, including requests for funding submitted by the City to HUD and/or submitted to the City by the DLDC to request CDBG funding
- o Bank statements and canceled checks or check images.

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

APPENDIX C

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