



U.S. Department of Housing and Urban Development
Wanamaker Building, Suite 1005
100 Penn Square East
Philadelphia, PA 19107-3380

District Inspector General for Audit

April 29, 1996

Audit Related Memorandum
No. 96-PH-249-1815

MEMORANDUM FOR: Joyce Gaskins, Director, Office of Community
Planning and Development, 3AD

FROM: Edward F. Momorella, District Inspector General
for Audit, Mid-Atlantic, 3AGA

SUBJECT: Limited Review - Delaware County CDBG Program
Penza Tract Fund
Media, PA

INTRODUCTION

We performed a limited review of the subject fund, which was established from proceeds of the sale of real property originally acquired by Delaware County (Grantee) with Community Development Block Grant (CDBG) funds. The purpose of the review was to determine whether the Penza Tract Fund, including interest earnings, represents program income due the CDBG program.

The review was performed in March 1996 and covered the period from January 1977 to the present. We reviewed documents from the HUD Philadelphia Office and from the Grantee.

SUMMARY

The Grantee sold land in 1979 and 1981 that had previously been acquired with CDBG funds, but did not credit the net sales proceeds of \$1,262,990 to program income, as required; and, earned a minimum of \$516,309 in interest on the land sales proceeds since April 1988, but did not credit these earnings to CDBG program income, as required. Part of these interest earnings were transferred to the Grantee's general fund and subsequently spent on general governmental activities, contrary to regulations.

We recommend you require the Grantee reimburse its CDBG fund \$1,779,299 for the sales proceeds and interest earned from April 1988 to December 1994. We also recommend your staff determine, based on the Grantee's records, the amount of interest earned on the sales proceeds after December 1994, and require the Grantee reimburse this amount to the CDBG program.

Because the conditions cited in this memorandum require corrective action, the finding will be controlled in accordance with HUD Handbook 2000.6 REV-2, Audits Management System.

Within 60 days please give us, for each recommendation made in the memorandum, a status report on: (1) the corrective action taken; or (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued because of the review.

BACKGROUND

Purchase of the Penza Tract

In 1977, the Grantee spent \$1,855,000 in CDBG funds from Program Years 2 and 3 to acquire, through condemnation, 56.6 acres of land known as the "Penza Tract".

The Grantee purchased this property, which is located adjacent to the county-owned Smedley Park in Nether Providence Township, ostensibly in order to prevent further development in an environmentally-sensitive area, and to make up for the anticipated loss of park land that would result from the planned completion of Interstate 476, known locally as the "Blue Route". The original owner of the Penza Tract, Nicole Enterprises, appealed the compensation amount.

The HUD Philadelphia Office originally disapproved the use of Year 3 funds to complete the acquisition, because it did not meet criteria set forth in CPD Notice 77-10 regarding compliance with the primary objectives of the program. The Philadelphia Office subsequently waived these requirements on August 5, 1977, based on its approval of the activity in the previous year's CDBG program and the financial hardship the Grantee would suffer as a result of a negative decision. The letter indicated, however, that the Grantee should make every effort to obtain funds for this activity from other resources.

Establishment of the Penza Fund

In December 1979, the Grantee sold 26.31 acres of Penza Tract land to the Pennsylvania Department of Transportation for \$1,884,600. On June 10, 1981 the Grantee sold an additional 1.27 acre area to the Department of Transportation for \$103,950.

3

The Grantee deposited these sales proceeds into a separate bank account and established on its books a separate capital projects fund account known as the "Penza Fund". The agreement of sale gave the Grantee the right of first refusal if the land was ever resold. At the time, the highway project had been delayed for a number of years by litigation and there was concern that it would never be built. The remainder of the Penza Tract (29.02 acres) was incorporated into Smedley Park.

In February 1981, a final settlement was reached with Nicole Enterprises requiring the expenditure of an additional \$725,560, which the Grantee disbursed from the Penza Fund account.

Completion of the Blue Route

The highway was constructed through the Penza land sold to the Transportation Department and through an eight acre section of Smedley Park, and was completed and opened to the public in December 1991. However, the Grantee continued to maintain the Penza Fund monies in an interest-bearing account. Grantee representatives told us that a portion of the Penza land sold to the Transportation Department, but not used for the highway, could still be offered back to the Grantee and that officials wanted funds to be available if this occurs.

Status of the Penza Fund

The Penza Fund has earned interest income from 1979 to the present time. Most of this income was transferred each year from the Penza Fund to the Grantee's General Fund and expended on general government activities. Grantee records show that a minimum of \$1,523,416 was transferred between 1982 and 1993. According to Grantee representatives there were no withdrawals from the Penza Fund in 1994 and 1995.

The Grantee also made withdrawals from the Fund to pay for park-related purposes, including maintenance and administration attributable to the Penza land. As of June 30, 1995, the Penza Fund account totaled \$2,139,716, which included \$734,095 deposited in 1989 from the sale of an unrelated parcel known as the Lawton Tract.

Grantee's Current Position

Grantee representatives acknowledge that at least a portion of the

Penza Fund represents CDBG program income and have offered to reimburse the CDBG program \$762,284 "once all contingencies have been satisfied", which apparently means once all Penza land not needed by the Department of Transportation has been repurchased by the Grantee. This figure is based on a pro-ration of the original \$1,855,000 in CDBG funds utilized for acquisition to the portion sold to the Department of Transportation, minus estimated park related expenses, as follows:

4

Original CDBG funds utilized	\$1,855,000
Pro-ration (26.31/56.6)	862,284
Less: Park-related expenses	<u>100,000</u>
Grantee's offer	<u>\$762,284</u>

Should you or your staff have any questions, please contact Richard J. DeCarlo, Assistant District Inspector General for Audit, at 656-3401.

Attachments

1. Results of Review and Recommendation
2. Schedule of Revenues and Transfers
3. Distribution

RESULTS OF REVIEW AND RECOMMENDATIONSProceeds from the Sale of Penza Tract Land

Grantee representatives told us that Delaware County officials strongly believed they had a moral commitment to their residents to reacquire Penza Tract land not needed for the highway, in order to prevent development at this environmentally-sensitive location. Although they acknowledged that the agreement of sale with the Department of Transportation did not require the Grantee to repurchase land, this "moral commitment" apparently became the basis for the establishment of the Penza fund.

The Grantee should have treated the proceeds from the sale of the Penza land to the Pennsylvania Department of Transportation as CDBG program income at the time of sale. The terms of the sales agreement did not require the Grantee to repurchase land not used for the highway. Although HUD approved the use of CDBG funds to pay for a land acquisition, there was no indication that this approval extended to the use of program income to fund a potential reacquisition.

According to the Grantee's representative, the \$725,560 settlement with the former owner of the Penza Tract was not paid from program income, but rather from the increase in land value from 1977 to 1979. The Grantee contends that when land was acquired with CDBG funds and subsequently sold at a higher price, Federal regulations

prior to 1988 did not require that the gain/difference be paid to the CDBG fund, which resulted in a windfall to the Grantee. However, 24 CFR 570.506 includes in the category of other program income proceeds from the disposition of real property. Other program income is income which must be retained by the recipient and spent on eligible program activities. Although the regulation did not require that land acquired with CDBG funds be sold at fair market value, it also did not specifically limit the amount of proceeds when the selling price exceeds the acquisition cost. Currently, 24 CFR 570.505 requires a Grantee to reimburse the CDBG program the fair market value when a property is sold or put to a new use that does not meet a national objective. Consequently, we believe that the entire land sales proceeds of \$1,988,550 must be considered program income. However, use of sales proceeds to pay the \$725,560 settlement amount to the former owner was appropriate because it was directly tied to the original condemnation transaction approved by HUD for CDBG funding.

6

Maintenance and Administrative Costs

Grantee officials presented no justification for deducting maintenance and administrative costs from land sales proceeds. 24 CFR 570.207(b)(2) provides that expenses for maintenance and repair of streets, parks, playgrounds etc. and for the payment of salaries for staff, utility costs and similar expenses necessary for the operation of public works and facilities are generally ineligible.

Interest Earnings

Regulations governing the CDBG program did not specifically address interest accumulated on program income held pending disposition until the 1988 revision at 24 CFR 570.500(a)(1)(ix) specifically included such earnings in the definition of program income. Therefore, all interest earned after April 1988, the date of the revised Code of Federal Regulations, should be included in program income.

OIG Position

We believe that the net sales proceeds should be treated as CDBG program income in accordance with current regulations, as follows:

Total Sales Proceeds	\$1,988,550
Less: Additional Settlement	<u>725,560</u>
Net Proceeds	\$1,262,990
Plus: Interest Earnings	<u>516,309</u>

Total

\$1,779,299

Interest earnings cover the period April 1988 to December 1994. These figures should be updated to the present, based on the Grantee's records, with no deductions for maintenance and administration.

The Grantee should be required to expend the \$1,779,299 plus interest earned after December 31, 1994 on eligible activities before it draws additional funds on its Letter of Credit.

Recommendations

We recommend that you require the Grantee to:

- A. Reimburse the CDBG program \$1,779,299, plus interest earned since December 31, 1994. These funds should be spent on eligible program activities before additional Letter of Credit drawdowns are requested.

Delaware County CDBG Program
Penza Tract Fund

SCHEDULE OF REVENUES AND TRANSFERS

<u>Year</u>	<u>Proceeds from Sale</u>	<u>Interest Earnings</u>	<u>Expenditures</u>	<u>Transfers from Fund</u>	<u>Interest Due Program</u>
1979	\$1,884,600	*	*	*	
1980		*	*	*	
1981	(725,560) 103,950	*	*	*	
1982		\$219,568		\$200,000	
1983		136,213		200,000	
1984		152,698		125,000	
1985		124,240		125,000	
1986		100,022		125,000	
1987		92,228		125,000	
1988		151,286		125,000	71,482 (1)
1989		190,971		125,000	120,312 (2)
1990		174,700		125,000	110,061 (2)

1991	129,212		125,000	81,404 (2)
1992	73,835	74,923	75,000	46,516 (3)
1993	59,693	2,596	48,416	37,607 (3)
1994	<u>61,789</u>	<u> </u>	<u> </u>	<u>38,927 (2)</u>
	<u>\$1,262,990</u>	<u>\$1,666,455</u>	<u>\$77,519</u>	<u>\$1,523,416</u>
				<u>\$516,309</u>

* Indicates data not available from records provided by the Grantee

Notes:

- (1) Grantee deposited a net amount of \$734,095 from the sale of an unrelated tract of land (Lawton Tract) into the Penza Fund during the year.

Interest due Program based on a 37 to 63 percent pro-ration which was the ratio of Lawton Tract net proceeds to Penza Tract net proceeds.

Amount due Program was based on 75 percent of interest earned on Penza proceeds during the year in order to reflect the period from April to December 1988.

- (2) Interest based on a 37 to 63 percent pro-ration which was the ratio of Lawton Tract net proceeds to Penza Tract net proceeds.

8

- (3) Information on expenditures was not available from records provided by the Grantee.

Interest based on a 37 to 63 percent pro-ration which was the ratio of Lawton Tract net proceeds to Penza Tract net proceeds.

Distribution

Secretary's Representative, Mid-Atlantic, 3AS
Internal Control & Audit Resolution Staff, 3AFI
Director, Field Accounting Division, 3AFF
Director, Office of Community Planning and Development, 3AD
Assistant to the Secretary for Field Management, SC (Room 7106)
Audit Liaison Officer, COM (Room 7228) (3)
Acquisitions Librarian, Library, AS (Room 8141)
Chief Financial Officer, F (Room 10166) (2)
Deputy Chief Financial Officer for Operations, FO (Room 10166) (2)
Associate General Counsel, Office of Assisted Housing and Community
Development, GC, (Room 8162)
Assistant Director in Charge, US GAO, 820 1st St., NE Union Plaza,
Bldg. 2, Suite 150, Washington, DC 20002
Attn: Mr. Cliff Fowler (1)
Mr. Paul G. Mattus, Chairman, Delaware County Council, Government
Center Building, Media, PA 19063



REPORT NAME: Limited Review - Delaware County CDBG
 Program
 Penza Tract Fund
 REPORT NO: 96-PH-249-1815
 ISSUE DATE: April 29, 1996

REGIONAL OFFICE (NON-OIG)		
	Secretary's Representative, Mid-Atlantic, 3AS	1
	Internal Control & Audit Resolution Staff, 3AFI	1
	Director, Office of Community Planning and Development, 3AD	1
	Director, Field Accounting Division, 3AFF	1
HEADQUARTERS (NON-OIG)		
	Assistant Secretary for Field Management, SC (Room 7106)	1
	Associate General Counsel, Office of Assisted Housing and Community Development, GC (Room 8162)	1

	Jo Ann Stanton, Audit Liaison Officer, COM (Room 7228)	3
	Acquisitions Librarian, Library, AS (Room 8141)	1
	Chief Financial Officer, F (Room 10166)	2
	Deputy Chief Financial Officer for Operations, F (Room 10166)	2
HEADQUARTERS (OIG)		
	Michael R. Phelps, Deputy Assistant Inspector General, GA (Room 8286)	1
	James M. Martin, Director, Program Analysis & Special Projects Division, GAP (Room 8180)	1
	Central Files, (Room 8260)	2
	Semi-Annual Report Coordinator (Room 8254)	1
DISTRIBUTION OUTSIDE HUD		
	Assistant Director in Charge, US GAO, 820 1st St. NE Union Plaza, Bldg. 2, Suite 150, Washington, DC 20002 Attn: Mr. Cliff Fowler	1
	Mr. Paul G. Mattus, Chairman, Delaware County Council, Government Center Building, Media, PA 19063	<u>1</u> <u>21</u>
	From: Edward F. Momorella, DIGA, Mid-Atlantic Wanamaker Building, Suite 1005 100 Penn Square East Philadelphia, PA 19107-3380	

CC:OSWALD

3AGA:DECARLO:AMP:04/18/96

Correspondence Code	3AGA			
Concurrence	DECARLO			
Date				

