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# AUDIT REPORT



HISTORIC WESTSIDE VILLAGE,  
SECTION 108 LOAN AND ECONOMIC  
DEVELOPMENT INITIATIVE GRANT  
CITY OF ATLANTA, GEORGIA

2003-AT-1004

JUNE 6, 2003

OFFICE OF AUDIT, REGION 4

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Issue Date	June 6, 2003
Audit Case Number	2003-AT-1004

TO: John Perry, Director, Office of Community Planning and Development, 4AD

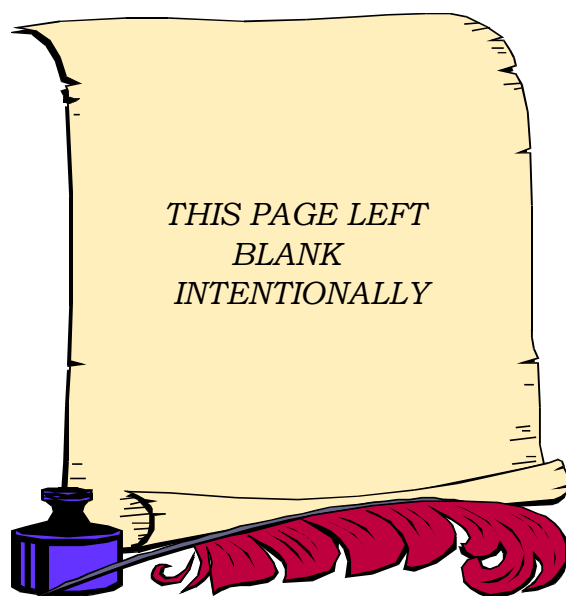
FROM: Nancy H. Cooper  
Regional Inspector General for Audit, 4AGA

SUBJECT: Historic Westside Village,  
Section 108 Loan and Economic Development Initiative Grant  
Atlanta, Georgia

We completed an audit of the City of Atlanta, Section 108 loan and Economic Development Initiative (EDI) grant for the Historic Westside Village. We conducted the audit at the request of your office. This report contains two findings that require follow-up by your office to implement appropriate corrective action.

In accordance with the Department of Housing and Urban Development (HUD) Handbook 2000.06 REV-3, within 60 days please provide us, for each recommendation without management decisions, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Additional status reports are required at 90 days and 120 days after report issuance for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the audit.

Should you have any questions, please contact Terry A. Cover, Assistant Regional Inspector General for Audit, or Narcell Stamps, Senior Auditor at (404) 331-3369.



# Executive Summary

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We conducted an audit of the City of Atlanta's administration of a Section 108 loan and EDI grant in response to a request from HUD's Georgia State Office, Office of Community Planning and Development (CPD). HUD provided a \$6,825,000 Section 108 Loan and a \$383,000 EDI grant to assist in funding the Historic Westside Village (Project.) Our audit objective was to determine if the City and its sub-recipient administered Project activities funded by the HUD loan and grant in accordance with program requirements. Those compliance requirements included maintaining adequate budgetary and accounting controls over Section 108 and EDI funded activities, managing sub-recipient activities, conducting competitive procurements, and expenditure of HUD funds for eligible, necessary, and reasonable Project costs.

The City of Atlanta (City) and its sub-recipient, the Atlanta Development Authority (ADA) did not adequately manage and control the Project. The City lost control of the Project and allowed significant violations of HUD requirements to occur without early detection or prompt corrective action. The City and ADA:

- Did not adequately monitor the performance of sub-recipients to ensure compliance with HUD program requirements. The City and ADA improperly allowed an ADA affiliate, Inner City Development Corporation (ICDC), to perform as a grant sub-recipient without executing a sub-recipient agreement to establish its responsibilities. ICDC improperly paid \$1.35 million of Section 108 funds for non-competitively selected service vendors. The \$1.35 million included \$143,369 of ineligible costs, and \$504,569 of inadequately supported costs identified by audit testing. We concluded there was little assurance the non-competitive expenditures were reasonable, project related, and eligible. Additionally, audit tests found that ICDC expended \$163,279 of Section 108 funds for other ineligible and unsupported costs. (See Finding 2 for details of ineligible and unsupported costs.)
- Did not competitively procure and execute a contract with a "for-profit" company, Historic Westside Partners, LLC (HWP), as the Project's exclusive development and management agent. The City and ADA allowed "for-profit" affiliates of HWP and ICDC to become exclusive developers with ownership interests in Project land and leases without competition, and without compensation to the City or the Section 108 Program.
- Lost ownership and control of Project land acquired with HUD funds. ICDC gave two land parcels to "for-profit" companies without compensation despite a City Council resolution directing that land be sold to repay the HUD loan and an ICDC Board resolution that a for-profit company would pay \$1.7 million for one parcel. ICDC also jeopardized future development of a third parcel by encumbering it to finance unrelated development on one of the parcels it gave away.
- Did not generate program income as pledged to HUD for loan repayment. The opportunity to collect at least \$1.7 million from one land parcel was not pursued and Project related revenues totaling \$403,603 were not properly recorded as Project revenue.

- Did not comply with HUD requirements pertaining to (a) competitive procurements of 22 services vendors, (b) Project budget approvals, and (c) Project accounting. The City did not obtain HUD approval for major changes in the Project scope and budget.

We recommend that HUD initiate sanctions against City, ADA, and ICDC officials responsible for serious program violations. We also recommended requiring the City to (1) provide evidence that its management control and accounting systems comply with HUD requirements before advancing any further funding (2) recover certain land parcels or appropriate program income from those parcels, and (3) repay Section 108 project accounts for \$1.35 million of non-competitively procured services, \$15,132 of other ineligible costs, and provide adequate support or repay \$148,147 of unsupported costs.

We discussed the audit findings and recommendations with the City and ADA officials during the audit and at an exit conference held on April 28, 2003.

HUD CPD officials agreed with the findings and recommendations. The City of Atlanta's written response was positive. It recognized the seriousness of the audit findings, presented a willingness to work with HUD to resolve the deficiencies, and cited constructive improvements in program management that have been made or are planned. However, some of the City's specific proposals do not adequately address the findings and do not conform to HUD regulatory requirements. The City's response is included in the report as Appendix F. Enclosures to the City's letter are not included due to their length, but were provided to HUD and are available upon request.

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### **Abbreviations**

ADA	Atlanta Development Authority
CFR	Code of Federal Regulations
City	The City of Atlanta, Georgia
CPD	Community Planning and Development
EDI	Economic Development Initiative
HWP	Historic Westside Partners, Limited Liability Company
HUD	U. S. Department of Housing and Urban Development
HWV3A	Historic Westside Village 3A, Limited Liability Company
ICDC	Inner City Development Corporation
LLC	Limited Liability Company
Project	Historic Westside Village

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# Introduction

HUD awarded the City of Atlanta a loan and grant totaling \$7,208,000 to assist in developing the Martin Luther King Boulevard/Ashby Street Commercial Revitalization Project that later became known as Historic Westside Village.

Description	Award Date	Amount
Section 108 Loan	December 6, 1994	\$6,825,000
EDI Grant	May 15, 1997	383,000
Total		\$7,208,000

HUD approved the Section 108 Loan to fund relocation, site clearance, public improvements, construction, financing, and administrative costs. The City pledged Community Development Block Grant and program income to repay the Section 108 Loan by August 2010. HUD approved the EDI Grant for facade improvements as a complement to the Section 108 Loan.

The City's Department of Planning, Development, and Neighborhood Conservation was responsible for implementing the Project. The City carried out the programs through its sub-grantee, ADA. The City replaced a previous sub-grantee, the Atlanta Economic Development Corporation, with ADA in June 1997. During the period audited, the previous City Mayor served as the Chairman of the Boards of Directors for both sub-grantees. Both sub-grantees used an affiliated entity, ICDC, as a sub-recipient. ADA officials stated that ICDC was a shell nonprofit corporation with no staff, which operated using ADA's staff and office facilities.

The Project started with the selection of H. J. Russell and Company as the primary developer. In March 1998, the City Council passed a resolution canceling the Russell contract through mutual consent. The resolution also authorized ADA to issue a request for proposals to select a new developer. ADA received only one response to the request for proposals from the Integral Group, LLC. ADA rejected the Integral Group proposal and decided to use ICDC as the primary developer. ADA selected several vendors, including the Integral Group, LLC, to participate as members of the Development Team.

Subsequently, HWP, an affiliate of the Integral Group, contracted with ICDC to be the exclusive development and management agent, with ICDC as the master developer. Appendix A presents a chart of the entities affiliated with ADA and the Integral Group that participated in Project development.

At the time of our audit, 8 years after the Project began and \$7.15 million of HUD funds were spent, achievements included acquisition and clearing of 16 acres, relocation of prior landowners and tenants, and construction of a major supermarket, video store, restaurant, and a proposed bank building on a 3-acre parcel. The supermarket and video store were in operation and a lease had been signed for the restaurant. The remaining 13 acres of Project land remained vacant. HUD program officials consider the completed shopping area to be a desirable community improvement. However, the Project is in jeopardy if the City does not meet contractual targets



for starting construction of additional developments. The supermarket's lease allows it to cancel operations if the target dates are not met.

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### Audit Objectives

Our audit objective was to determine if the City and its sub-recipient administered Project activities funded by the HUD loan and grant in accordance with program requirements. Those compliance requirements included maintaining adequate budgetary and accounting controls over Section 108 and EDI funded activities, managing sub-recipient activities, conducting competitive procurements, and expenditure of HUD funds for eligible, necessary, and reasonable Project costs.

### Audit Scope and Methodology

To accomplish our objectives, we performed the following reviews and tests:

- Reviewed HUD, ADA, and ICDC Project records and funding agreements at their respective offices in Atlanta, Georgia.
- Performed public records searches at the Secretary of State's Office, the local courthouse, and online databases.
- Interviewed HUD, City, and ADA/ICDC officials and staff, including former ADA staff as needed to gather information and discuss questions and potential audit issues.
- Met with the current City Mayor and City and HUD officials to discuss potential findings related to control of Project land and Section 108 program income.
- Visited and observed the completed and in-process developments at the Project site located on Martin Luther King Drive, Atlanta, Georgia.
- Compiled Project costs by activity from analysis of detail cost information attached to payment requests ADA submitted to the City, and reconciled associated payments to the City's general ledger entries.
- Reviewed City, ADA, and ICDC general ledgers for adequacy of accounting data and to identify potential program income.
- Confirmed lease payments with tenants occupying space constructed on Project land.

- Examined 45 percent of \$167,859 the City paid directly to program vendors, and \$3,916,250 of acquisition costs for 93 of 116 acquired land parcels. ADA could not locate records for the remaining 23 parcels.
- Examined a non-representative sample of other costs (Project management, architect and engineering, legal, and other consultants) totaling \$1,029,838. Because City and ADA accounting records were deficient, we selected five ADA reimbursement requests paid by the City that contained the \$1,029,838. The five requests were selected based on high dollar amount, and their inclusion of a variety of costs including costs of concern to HUD.
- Traced the selected costs to supporting documents (contracts, invoices, cost justifications, and/or other documents) and to cancelled checks and/or bank statements to confirm payment and amounts.
- Assessed the adequacy of the City's monitoring of sub-recipients and Project activities, and the adequacy of accounting and budgetary controls and records.

Our audit generally covered Project development activities during the period December 1, 1994 through May 31, 2002. Coverage was extended through December 2002 to identify potential program income. We performed the audit from May 2002 through March 2003. We conducted the audit in accordance with generally accepted government auditing standards.

We provided a copy of this report to HUD's Assistant Secretary for Community Planning and Development and to the Mayor of the City of Atlanta.



## Inadequate City and ADA Management of Project Development

The City of Atlanta and its sub-recipient, ADA, did not adequately manage and control the Project and \$7,208,000 of HUD funding. The City lost control of the Project and allowed significant violations of HUD requirements to occur without early detection or prompt corrective action. The City and/or ADA:

- Did not adequately monitor the performance of ADA and ICDC, an ADA affiliate, to ensure compliance with HUD program requirements. ICDC improperly paid \$1.35 million of Section 108 funds for non-competitively selected service vendors. The \$1.35 million included \$143,369 of ineligible costs, and \$504,569 of inadequately supported costs, identified by audit testing. We concluded there was little assurance the non-competitive expenditures were efficient, project related, and eligible costs. Additionally, audit tests found that ICDC expended \$163,279 of Section 108 funds for other ineligible and unsupported costs. (See Finding 2 for details of ineligible and unsupported costs.)
- Did not execute a sub-recipient agreement with ICDC to establish its authority and responsibility as a grant sub-recipient.
- Did not execute a contract with the “for-profit” company, HWP, as the project’s exclusive development agent. The City and ADA then allowed “for-profit” affiliates of HWP and ICDC to become exclusive developers with ownership interests in Project land and leases without competition, and without compensation to the City or the Section 108 Program.
- Lost ownership and control of Project land acquired with HUD funds. ICDC gave two land parcels to “for-profit” companies without compensation despite: (1) a City Council resolution directing that Project land be sold to repay the HUD loan, (2) an ICDC Board resolution that a for-profit company would pay \$1.7 million for project Block 2A, and (3) agreements with HUD pledging program income to repay the Section 108 loan. ICDC also jeopardized future development of a third parcel (Block 1) by encumbering it to finance unrelated development on Block 3A. Therefore, Block 1 is not available to secure debt financing for its development.
- Did not generate program income pledged to HUD for loan repayment.
- Did not comply with other HUD requirements pertaining to (a) competitive procurements, (b) Project budget approvals, and (c) Project accounting. The City did not obtain HUD approval for major changes in the Project’s scope and budget.

These conditions occurred because (1) the City, and the ADA and ICDC Boards of Directors did not adequately monitor and manage project activities, and (2) City and ADA officials disregarded HUD regulatory requirements.

Program requirements

Grantees are responsible for managing the day-to-day operations of grant and sub-grant supported activities, to assure compliance with applicable Federal requirements and achievement of performance goals. (Title 24 Code of Federal Regulations (CFR) Part 85.40(a).)

All procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of Section 85.36. Situations restricting competition include noncompetitive pricing practices between firms or between affiliated companies and organizational conflicts of interest. (24 CFR 85.36 (c).)

Grantees and sub-grantees must maintain records that adequately identify the source and application of funds provided for financially assisted activities. These records must identify grant or sub-grant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income. Actual expenditures or outlays must be compared with budgeted amounts for each grant or sub-grant (24 CFR 85.20 (b).) Grantees and sub-grantees are required to maintain financial records, supporting documents, statistical records, and all other records pertaining to the project for 3 years from the date of the final expenditure report or until after all litigation, claims, or audit findings started before the expiration of the 3-year period, have been resolved (24 CFR 85.42.)

A. The City did not adequately manage and monitor the sub-recipients and project

The City did not adequately manage and monitor performance by ADA and ICDC. On June 12, 2000, HUD issued a report citing the City's inadequate monitoring of ADA. Our audit confirmed HUD's findings and disclosed additional compliance deficiencies.

The City conducted only two limited scope reviews of ADA and Project activities. The City reviewed ADA's acquisition and relocation activities in November 1999 and concluded that ADA had complied with program requirements. In response to HUD's report, in November 2000 the City reviewed procurement issues raised by HUD, and concluded that ADA had not complied with competitive procurement procedures. Our audit confirmed

HUD's findings and identified additional Project management and compliance deficiencies. The City should have detected the compliance violations had it properly monitored the Project, and ADA and ICDC performance.

City staff stated that the prior City Commissioner for the Department of Planning and Community Development and the former Mayor's office obstructed their efforts to monitor the Project. We also observed that ADA's Board, chaired by the prior Atlanta City Mayor, did not provide adequate oversight of the Project. We found no evidence that ADA officers presented key issues to the Board for their review and approval. The Board minutes provided little or no information on Project decisions such as major changes in Project scope and budget, noncompetitive procurements, authorizations of contract awards, and participation by affiliated for-profit companies. Furthermore, ICDC either did not maintain Board minutes or choose not to provide the minutes as we requested. We found little evidence that the ADA and ICDC Boards were actively involved in Project decisions. ADA staff indicated that there were few ICDC Board meetings. We found minutes for only one Board meeting and two Board resolutions drawn up and signed by ICDC officers without Board meetings. We concluded that ADA's officers, who also served as ICDC officers, controlled the Project with little oversight from their Boards and the City.

B. ADA improperly gave sub-recipient authority to ICDC without a contract, and ICDC did not comply with sub-recipient requirements

The City and ADA allowed ICDC, a non-profit entity affiliated with and controlled by ADA, to act as a sub-recipient and developer without a sub-recipient agreement. Without this agreement, ICDC should not have held title to Project land, executed Project contracts, and disbursed Project funds to third parties.

Before disbursing any funds to a sub-recipient, the recipient shall sign a written agreement with the sub-recipient, which shall remain in effect during any period that the sub-recipient has control over program funds, including program income. The agreement shall include a description of the work to be performed, a schedule for completing the work, and a budget. These items shall be in sufficient detail to provide a basis for the recipient to effectively monitor performance (24 CFR 570.503.)

### ICDC Participation Was Questionable

ADA officials stated that ICDC was a shell entity with no employees and that ICDC operated using ADA staff and office facilities. ADA's president was also the president of ICDC, and other ADA officers were also ICDC officers. ADA's and ICDC's accounting ledgers did not allocate any ADA costs such as staff salaries and office costs to ICDC.

ICDC's Bylaws show that it was a 501(c)(3) tax-exempt nonprofit organization. However, ADA and ICDC could not produce the required Internal Revenue Service tax exemption letter. Also, ICDC did not file required annual nonprofit tax returns. Thus, we could not confirm that ICDC was an approved tax-exempt entity.

### ICDC Did Not Comply With Sub-recipient Requirements

ICDC did not obtain annual audits as is required of sub-recipients (Office of Management and Budget Circular A133, Section 210.) ADA/ICDC officials stated that they did not know ICDC was required to obtain annual audits.

ICDC did not maintain accounting ledgers identifying the source and use of funds and program income. Expenditures claimed for reimbursement from HUD funding were not identified in ICDC's accounting ledger as to source of funds, and thus, there was no assurance that the same costs were not also claimed against other fund sources (e.g., empowerment zone funds, City funds, and a private loan.) Our audit tests identified some duplicate claims (see Finding 2.) Further, ICDC's accounting records did not identify any Section 108 Program income. Our audit identified income transactions that were not properly accounted for (see Section E below.)

ICDC also maintained ledger accounts for its two subsidiary for-profit companies that became the owners of project land. However, those records were materially incomplete. No real property asset values were recorded for project land (Blocks 2A and 3A) that was transferred to the two entities. The October 2002 ledger for one of the companies Historic Westside Village 3A, Limited Liability Company (HWV3A, LLC) recorded \$65,000 of rent collected for the period May 2002 through October 2002

C. “For-Profit” companies  
improperly received fees  
and ownership interests

from business tenants on Block 3A. However, the \$65,000 represented a net amount received from a leasing agent after deduction of management fees and other costs incurred by the leasing agent. HUD regulations and generally accepted accounting principles require a company’s accounting records to include all relevant assets, revenues, and expenses, versus net amounts.

ADA advertised a request for proposal for a project developer and received one response from the Integral Group, LLC. Integral Group, LLC proposed to purchase all project land for \$2,374,275. ADA rejected the proposal and decided to become the developer through its non-profit affiliate, ICDC. ADA then invited Integral Group to participate in the project as a member of the development team.

Subsequently, HWP, an affiliate of the Integral Group, was given contract rights as the exclusive “for-fee” development and management agent and rights to become an owner of Project components. The City and ADA did not execute any contracts with HWP and Integral Group. Instead, contract rights were granted in a contract between ICDC and HWP. Since neither the City nor ADA had a contract with ICDC, ICDC had no authority to perform as a grant sub-recipient and no authority to execute contracts involving HUD funded activities.

The “Program Management and Development Agreement” between ICDC and HWP designated ICDC as the master developer and HWP as the exclusive for-fee development agent. The agreement also named 12 other firms to be consultants and members of the development team. Under the agreement, ICDC paid HWP \$373,157 for management fees reimbursed from HUD funds. We found at least \$84,136 was ineligible and unnecessary (see Finding 2.)

The agreement stipulated that ICDC and HWP would assume ownership roles in businesses subsequently formed to own and operate various Project components. ICDC and the Integral Group formed two for-profit companies to own and develop Project land. ICDC then transferred Project land to the two for-profit companies without any compensation to the City or the Section 108 Program (see discussion below.)



See Appendix A for a flowchart of the participating entities affiliated with the Integral Group, LLC and ICDC, and further ownership information.

**D. The City and ADA did not control ownership of Project assets**

The City and ADA improperly allowed ICDC to hold title to Project real property, and to encumber and transfer ownership of real property without compensation to the City or the Section 108 Program. This deprived the City of income needed for repayment of the Section 108 loan as pledged, or with HUD approval, for Project development.

Title to real property acquired under a grant or sub-grant will be vested upon acquisition in the grantee (the City) or sub-grantee (ADA.) The grantee or sub-grantee shall not dispose of or encumber its title or other interests in the property (24 CFR 85.31.)

During calendar year 2000, the City quit claimed 45 parcels of land to ICDC. ICDC was also allowed to use Section 108 funds to purchase Project properties directly in its name. ICDC then transferred and/or encumbered 9 of 16 acres acquired for the Project to affiliated for-profit companies as shown below.

<b>Project Land</b>	<b>Total Acres</b>	<b>Acres Owned by ICDC</b>	<b>Acres Transferred or Encumbered</b>	<b>Transferred to</b>	<b>Acres Encumbered and Reason</b>
Block 1	4.241	4.241	4.241		Land encumbered for Block 3A development loan to HWV3A, LLC
Block 2A	1.338		1.338	HWV2A, LLC	Not encumbered *
Block 3A	3.513		3.513	HWV3A, LLC	Land encumbered for development loan to HWV3A, LLC
Remainder	6.984	6.984			Not encumbered
<b>Totals</b>	16.076	11.225	9.092		
* Plans were in process to encumber Block 2A.					

ICDC encumbered Block 3A and Block 1 to secure debt financing for Block 3A's development. As result, the Block 1 site will not be available to secure debt financing needed for its development.

ICDC and affiliates of the Integral Group formed two for-profit limited liability companies (LLCs) to construct buildings and own commercial activities on Blocks 2A and 3A. ICDC transferred ownership of project land and leases

to the two LLCs without any compensation to the City or the Section 108 program. ICDC received an 80 percent interest in the for-profit LLCs. Affiliates of the Integral Group received 20-percent ownership interests in the LLCs, and in Project land and leases with only a nominal \$100 capital contribution. ICDC was also supposed to contribute \$1.7 million to the Block 3A LLC, per the LLC operating agreement. However, ICDC did not contribute the \$1.7 million.

E. Planned program income was not generated

ADA disregarded loan agreements with HUD, and a City Council resolution to generate program income to partially repay the Section 108 loan. The City's Section 108 note with HUD pledged program income to repay the loan. A City Council resolution dated March 16, 1998, required ADA to generate sufficient income to repay the Section 108 loan, and an ICDC Board resolution required a for-profit company to pay \$1.7 million for the Block 2A land.

ADA had opportunities to generate program income. ADA advertised a request for proposal for a Project developer stipulating that the selected developer would pay \$2,374,275 for the Project land. In August 1998, the Integral Group, LLC, submitted the only response to the request for proposal, and agreed to the purchase price. However, in December 1998 ADA rejected the proposal and decided to become the developer through its non-profit affiliate, ICDC. Subsequently, the City and ADA made no contract arrangements to generate program income.

A May 30, 2001, consent resolution by ICDC's Board provided that a LLC company was to pay \$1.7 million for Project land (Block 2A.) ADA and ICDC arranged for the LLC to borrow \$1.9 million from the City's Urban Residential Finance Authority to purchase the land and pay loan costs. However, ICDC and the LLC instead used the loan proceeds to pay unrelated construction costs on a different parcel (Block 3A.) The City next approved \$5 million of City Tax Allocation District bonds to finance development of Block 2A. The allocation specifically set aside \$1.9 million for the LLC to purchase Block 2A. In December 2001, the LLC obtained the \$1.9 million, but used it to pay off the Urban Residential Finance Authority loan. Since the bonds are repaid from future City tax revenues, the City essentially gave \$1.9 million to the LLC,

a for-profit company, and lost \$1.7 million that was to be generated from Block 2A as program income. The remaining bond allocation had not been disbursed at the time of our audit inquiries.

We identified \$403,603 in Project revenues that neither ADA nor ICDC had recognized and recorded as project revenue. Such Project revenue should have been partially allocated as Section 108 Program income in accordance with HUD regulations.

Type of Revenue	Amounts
Monthly Lease Payments	\$ 236,994
Lease Termination fee	72,641
ADA Development fee	93,968
<b>Total</b>	<b>\$ 403,603</b>

Commercial leases on Block 3A generated the cited monthly lease revenues through December 31, 2002. The lease termination fee was collected when a Block 3A tenant cancelled its lease. ICDC recorded the termination fee as general revenue, but not as Project revenue. ADA improperly collected development fees from ICDC. As the City's sub-grantee, ADA is prohibited from collecting developer fees. HUD regulations require such fees to be treated as program income (24 CFR 85.22.)

The City submitted a proposed funding agreement to HUD dated September 10, 2001, proposing that ICDC pay up to \$4 million from sales of housing units proposed on Project land (\$2 million in cash and \$2 million in 30 year notes.) The document further proposed to release City liens on Project land that had commercial developments completed or planned. HUD refused to consider the agreement pending completion of this audit. This proposed agreement would eliminate the potential for program income from commercial developments, and add about \$11,000 to the cost of each proposed housing unit. The proposed release of City liens applies to land ICDC transferred to for-profit companies without compensation and/or encumbered with private debts. Any City liens on these lands would have minimal subordinate value. Currently, all program income is pledged to repay the Section 108 loan. HUD's loan security would be materially reduced if commercial developments were released from any consideration of generating program income.

F. Non-compliance with procurement, budget approval, and accounting requirements

The City and ADA disregarded competitive procurement requirements, substantially revised the Project scope and budget without obtaining the required HUD approval, and did not maintain sufficient accounting records to identify Project assets and expenditures by source of funding and budget classifications. Significant accounting records and support documents were also missing.

Noncompetitive Procurement of Contract Goods and Services

ADA and ICDC disregarded competitive procurement requirements in their purchase of Project services. ADA and ICDC paid \$2.5 million from Project funds for services provided by 22 pre-selected and non-competitively selected vendors. This included \$1.35 million paid from HUD funds. ADA had no evidence that its Board of Directors reviewed and approved the non-competitive selection of vendors. See Appendix B for a listing of the 22 vendors, costs incurred, and costs paid with HUD funds.

Non-Compliance With Section 108 Budget

The City and ADA substantially revised the Project's scope and projected costs without obtaining HUD's approval. They increased the scope and financing from an initial estimate of \$16.8 million to \$140 million. As of our review, the City and ADA had spent 99 percent of the Section 108 loan and the entire EDI grant, but had not completed the shopping center development called for by the original plan. City officials stated that they planned to submit one overall budget revision to HUD for all the changes made to the Project. Such approval was required before the City expended HUD funds on revised activities.

Grantees must obtain HUD approval to carry out an activity not previously described in its application to HUD or to substantially change the purpose, scope, location, or beneficiaries of an activity (24 CFR 570.704(c)(5).) Actual expenditures or outlays must be compared with budgeted amounts for each grant or sub-grant (24 CFR 85.20 (b)(4).)

The City did not and could not compare actual costs to the Project budget because accounting records were not properly maintained. Thus, the City and HUD were unable

## Finding 1

to properly monitor and control Project expenditures. HUD requested this audit because, among other concerns, the City could not provide HUD with an adequate accounting for program funds expended. We compiled expenditure classifications from payment request documents that ADA submitted to the City, and compared them to the approved budget in the table below. We did not audit the claimed cost classifications, but did note misclassifications.

Budget Line Item	HUD Approved Section 108 Budget	Expenditures Claimed (Unaudited)	Over Budget	Under Budget
Acquisition		\$ 3,992,588	\$ 3,992,588	
Relocation	\$ 201,250	520,265	319,015	
Site Preparation & Lighting	1,325,000	563,163		\$ 761,837
Construction Development	4,390,950			4,390,950
Public Improvements (Public Works)	500,000	500,000		
Administration	300,000	344,006	44,006	
Loan Processing Fee	107,800			107,800
Pre-Development		794,399	794,399	
Facade Improvement		10,229	10,229	
Section 108 loan interest payment		50,180	50,180	
<b>Totals</b>	\$ 6,825,000	\$ 6,774,830	\$ 5,210,417	\$ 5,260,587

As shown above, the City significantly deviated from the HUD approved budget. Furthermore, we identified significant misclassifications in amounts claimed as public works. The City claimed \$500,000 as public works costs, but the costs included no public works activities. Instead, the \$500,000 consisted of additional management and other service costs, and was a further deviation from the budget. The City claimed other similar costs as pre-development costs.

Type Services	Costs Claimed As Public Works
Program Management	\$ 195,475
Engineering	182,610
Legal	74,853
Consultant	47,062
Total	\$ 500,000

The City also used \$50,180 in HUD funds to make an unbudgeted interest payment on the Section 108 loan. City officials stated they used HUD funds because at the time the City did not have money for the payment. The City's contract with HUD pledged to repay the Section 108 loan

with its Community Development Block Grant funds and Section 108 Program income.

#### Non-Compliance With EDI Budget

The City also changed the purpose of the EDI grant from a facade improvement program to land acquisition and relocations without the required HUD approval. Acquisition was an eligible activity, but the change in program scope and budget required HUD's approval. City officials stated that they submitted a request to HUD for a budget amendment but they could not locate it and HUD officials stated that they never received it.

#### Inadequate Accounting Records

The City and ADA did not maintain required accounting records identifying Project expenditures by fund source and by HUD approved budget activity. Their accounting ledgers did not properly identify (1) expenditures charged to the \$7,157,830 Section 108 loan and EDI grant, (2) actual costs for comparison with budgeted costs and (3) the cost of Project assets (real property acquisition and improvement costs.)

The City maintained a general ledger that recorded all expenditures in two general accounts as shown in the table below.

Account Number	Account Description	Amount	EDI Grant	Total
529002	Service Grants	\$ 6,764,330	\$ 383,000	\$ 7,147,330
524001	Consultant Services	10,500		10,500
<b>Total</b>		\$ 6,774,830	\$ 383,000	\$ 7,157,830

A City official explained that they consolidated expenditures in the two general accounts for simplicity rather than account for each activity separately. The grant agreement with HUD cited the accounting requirements.

ADA's general ledger did not contain any accounts for Project assets, expenditures, and program income. ADA limited its Project accounting to a single receivable account that it used to record advances to ICDC and subsequent reimbursements from the City for costs incurred. ADA officials, who were also officers of ICDC, stated that they were not aware of required accounting procedures. ADA's

sub-recipient agreement with the City cited the accounting requirements.

#### Missing ADA and ICDC Records

ADA and ICDC could not find and provide us with general ledgers for 1994 through 1997, minutes for Board of Directors meetings held by ICDC and the Atlanta Economic Development Corporation (ADA's predecessor organization), and contracts with six vendors. Additionally, ADA and ICDC could not locate acquisition cost records for 23 properties acquired with HUD funds (see Finding 2.) The missing records deprived the City and HUD of information needed to assess ADA performance and the Board of Directors knowledge and approval of decisions made concerning the Project.

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#### City of Atlanta Comments

"The City and ADA are concerned about the findings of the Office of Inspector General regarding the actions of former officials. However, without further information regarding the nature and implications of what administrative sanctions HUD may impose, we must reserve comment.

"The City of Atlanta and the Atlanta Development Authority are in basic agreement with the OIG assessment that tighter accounting procedures, systems and controls are needed in regards to the HWV project and welcomes increased HUD monitoring of the project.

"The City disagrees that future Community Development Block Grant funding be withheld from the City as it believes its already has adequate accounting systems, procurement controls and monitoring systems with regards to its CDBG [Community Development Block Grant] projects. The audit examined only one Section 108 project, which involved unique development challenges, many funding sources and multiple partnerships. The HWV project remains distinctive from the City's annual CDBG grant processes.

"The City of Atlanta and ADA respectfully disagree with this recommendation [1C], at least in respect to the development of Parcels 3A, 2A and 3C. As indicated

above, delays in the project may result in the loss of Publix as an anchor tenant. The removal of ICDC from the project would basically unwind all progress to date and force the City and ADA to start the project over. This of course would cause great delay; void the private financing already obtained for these phases and effectively kill the project.

“Alternatively, the City proposes that ICDC be allowed to remain in the project for Phase 3A, 2A and 3C and that the City and ADA will prepare a Request for Proposals prior to the commencement of any subsequent phases.

“The City and ADA agrees with the OIG that the City should have received compensation when the land was transferred to the two limited liability corporations. However, to accept OIG recommendation to recover ownership appropriate income for Block 3A is not practical without risking the loss of the anchor tenant and the entire project. The private financing would have to be paid or collateralized from another source not currently available to either ADA or the City. Greater flexibility is available for Block 2A as construction has not yet begun. As such the City and ADA propose the following:

- “The ADA and ICDC will amend its partnership agreement for Block 3A. Cash flow generated from Block 3A will be divided between the City and ICDC in a 60% and 40% split respectively. The HWV3A LLC, and the ADA and ICDC Board of Directors have approved this sharing of cash flow. The agreement will be presented to the Atlanta City Council for approval within 45 days of acceptance of the proposal by HUD.
- “The HWV 2A Operating Agreement required HWV 2A to pay \$1,700,000 for the land acquisition. After the reconstruction of the general ledger and an independent audit to determine the actual cost of the Block 2A parcel, this provision of the Operating Agreement will be amended to reflect the true acquisition cost of the land. HWV 2A will then repay the actual acquisition cost of this parcel to the City as program income. In the event the land acquisition cost cannot be repaid in full, the ICDC Board of Directors has approved a resolution allotting 25% of the net cash flow from the development of the Block 2A parcel to the City as program income.



- “For all future phases of the Historic Westside Village project, the City will take all steps necessary to record and receive appropriate program income from each phase of the project.

“The City and ADA disagree with the OIG’s premise and recommendation [1E]. ICDC has in fact contributed the amount of \$1,990,000 in funds from the Tax Allocation District. Further the Urban Residential Finance Authority has guaranteed a private loan in the amount of \$4,000,000. Any confusion surrounding this contribution was caused by the delay in tax allocation district (TAD) funding to the project. \* \* \* To provide further clarification the development agreement for HWV3A, LLC has been amended to remove reference to the required \$1.7 million contribution.

“The City does agree that the encumbrance of Block 1 for the Block 3A project was inappropriate and should be removed. Whether or not it is feasible to remove this encumbrance is subject to negotiation with the bank providing the private financing for Block 3A. The City and ADA will explore its options with the bank immediately.

“The City of Atlanta and ADA agree with this recommendation [1F] and will transfer the referenced program income to the Section 108 project cash account as soon as the audit of ICDC, verifying this amounts, is completed.”

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## OIG Evaluation of City Comments

Overall, the City response recognizes the seriousness of the audit findings, presents a willingness to work with HUD to resolve the deficiencies, and cites constructive improvements in program management that have been made or are planned. Some to the City’s specific proposals do not adequately address the findings and do not conform to HUD regulatory requirements.

HUD will be responsible for implementing, and has agreed with recommendations 1A and 1B. The City disagreed with Recommendation 1B stating that it has proper controls

in place over CDBG projects. However, the City and ADA circumvented established internal controls in administering the Section 108 loan and EDI grant. We did not recommend that funds be withheld, rather that the City be required to demonstrate that adequate control processes are in place before funds are advanced. HUD may require the City to demonstrate its planned controls when circumstances warrant for specific proposed uses of HUD funds. We have revised the recommendation to eliminate a specific reference to CDBG funds and to reflect the need for HUD to emphasize controls over loan and grant funds when warranted by the planned use of funds.

In response to recommendation 1C, the City has improved its controls over ICDC and proposes to continue the project with ICDC as the master developer for Blocks 2A, 3A, and 3C, citing the possibility of undesirable consequences if it is removed. The City does not address prohibiting expenditures of HUD funds under the improper contract between ICDC and HWP. We are not recommending that the City stop scheduled development on Block 2A where contractual deadlines are in place with a bank and an existing anchor tenant. However, the management and development contract between ICDC and HWP contains numerous provisions that are prohibited by HUD regulations, and further development involving HUD funds and project land purchased with HUD funds cannot be allowed under that contract. The new contract between ADA and ICDC does not cure the improper contract between ICDC and HWP. The City should execute a proper sub-recipient agreement with ICDC specifically addressing its future involvement in existing and scheduled developments on Blocks 2A and 3A, and submit it for HUD review. All additional project development must be under a new development contract that complies with HUD regulations. The City should submit new development contracts for review by HUD. The City should also closely oversee the existing developments on Block 3A and scheduled developments on Block 2A. Furthermore, the City appears to be proposing development of Block 3C under the improper ICDC/HWP contract. At the time of our audit, the City and ADA did not disclose any contract granting development rights on Block 3C. HUD should not allow development of Block 3C under the improper ICDC/HWP contract. We have revised recommendation

1C for clarity and to specify that further development of land purchased with HUD funds should not be performed under the improper ICDC/HWP contract.

For recommendation 1D, the City proposes various program amendments including changes in ICDC's ownership interest in the two LLCs that own Blocks 2A and 3A, a potential payment by one LLC to purchase Block 2A, and pledges of stated percentages of cash flow from commercial developments on Blocks 2A and 3A as program income. The proposed purchase of Block 2A is uncertain, and the City does not indicate what factors will determine whether the LLC will or will not purchase Block 2A. HUD regulations would allow the City to determine Section 108 program income based on net income generated by commercial activities. However, the City proposal to base program income on arbitrary percentages of cash flow does not comply with the regulation and would be subject to arbitrary decisions on cash flow. The City needs to work with HUD to develop an allowable plan for program income on Blocks 2A and 3A.

In response to recommendation 1E, the City states that ICDC contributed \$1.9 million to develop Block 3A, and that the LLC agreement has been amended to eliminate the required \$1.7 million contribution by ICDC. As cited in the audit finding, the City Tax Allocation District contributed \$1.9 million for the LLC to purchase Block 2A. ICDC diverted those funds to repay a prior loan to the LLC. That prior loan was also earmarked to purchase Block 2A, but was diverted to develop Block 3A, depriving the City and the Section 108 Program of \$1.7 million in program income. No capital was contributed by ICDC. Removing the requirement for ICDC to contribute capital is not responsive to the audit findings and recommendation, and HUD should not accept the diverted funds as an acceptable contribution by ICDC.

The City agreed with recommendation 1F, and should provide HUD with documentation of its determination of program income amounts and transfer of funds to project accounts.

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**Recommendations**

We recommend that HUD:

- 1A. Initiate administrative sanctions against officials of the City, ADA, and ICDC who allowed violations to occur. This should include consideration of limited denials of participation and debarments.
- 1B. Before future loan and grant funds are advanced to the City and ADA and as needed based on planned uses of HUD funds, require evidence of 1) adequate accounting systems and procedures, 2) adequate procurement procedures and controls, 3) controls to monitor compliance with Federal funding requirements, and 4) adequate City and Board oversight of ADA. HUD should monitor procurements and Board minutes during Project planning and development stages, until the City and ADA have demonstrated compliance.

We further recommend that HUD require the City of Atlanta to:

- 1C. Prohibit ADA and ICDC from expending any HUD funds, including further developing land purchased with HUD funds, under the improper project management and development contract between ICDC and HWP.
- 1D. Recover ownership of Project land or appropriate program income from the transferred lands to repay the Section 108 loan or, with written HUD approval, for future Project development. This includes the \$1.7 million ICDC should have collected for the Block 2A site.
- 1E. Require ADA and/or ICDC to contribute the \$1.7 million ICDC agreed to contribute to the Block 3A component, and seek to remove the related encumbrance of Block 1.

- 1F. Require ICDC and ADA respectively, to record the \$72,641 lease termination fee and the \$93,968 developer fees as project revenue, and Section 108 Program income in accordance with HUD regulations. Require program income to be transferred to the Section 108 project cash account.

## The City and ADA Did Not Effectively Control Project Expenditures

The City and ADA did not effectively control Project expenditures to ensure they were eligible, reasonable, and supported. ADA and ICDC improperly expended \$1,350,116 of Section 108 funds for non-construction services from 22 non-competitively selected vendors. The City and ADA had no contracts with four of these vendors. Without competitive procurements, there is no assurance these costs were reasonable. Our audit tests of a sample of these costs identified \$143,369 of ineligible expenditures and \$504,569 of inadequately supported expenditures, providing little assurance that the service costs were eligible and project related. Our audit also identified \$144,447 in excessive, inadequately supported land acquisition costs, \$3,700 of inadequately supported legal costs, and \$15,132 of ineligible relocation costs. These conditions occurred due to inadequate City and ADA monitoring and control of Project operations (see Finding 1.) As a result, the City and ADA expended Project funds for ineligible, unsupported, and/or unreasonable costs.

### Program requirements

All procurement transactions will be conducted in a manner to provide full and open competition. Restrictions to competition include, but are not limited to: noncompetitive pricing practices between firms or between affiliated companies, organizational conflicts of interest, and any arbitrary action in the procurement process. The proposed procurement should be reviewed to avoid purchase of unnecessary or duplicative items. Records should be maintained to document the significant history of procurements. The records will include information such as the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price. (24 CFR Part 85.36.)

A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. Consideration shall be given to factors such as whether the costs are necessary, arms length transactions, and reflective of market pricing for comparable goods or services. The requirements further provide that the procurement must reflect prudent actions by individuals with consideration to their responsibilities to

the public and local and Federal Governments (Office of Management and Budget Circular A-87, Attachment C (2).)

### ADA disregarded required procurement procedures

ADA disregarded competitive procurement requirements in the purchase of project services. ADA and ICDC selected 22 vendors without following competitive procurement requirements. We reviewed ADA Board of Director's minutes and found no board review and/or approval to contract with the 22 vendors. ADA paid and was reimbursed \$2.5 million by the City, including \$1.35 million reimbursed from Section 108 funds, for costs billed by these vendors. See Appendix B for a list of the 22 vendors and amounts paid to each.

Non-Competitive Procurements			
Type Services	Number of Vendors	Costs Reimbursed by the City	Costs Reimbursed With Section 108 Funds
Program Management	4	\$ 684,854	\$ 373,157
Architects and Engineers	3	856,998	466,861
Environmental Services	1	343,284	49,659
Consultants	11	289,621	165,119
Legal Services <sup>1</sup>	3	336,769	295,320
Totals	22	\$2,511,526	\$1,350,116
<sup>1</sup> There were no contracts with three legal services vendors.			

ADA's Director of Commercial Development stated that he treated the Project as a private development and was not aware of any Federal procurement requirements. ADA's sub-recipient contract cited requirements for procurements and compliance with HUD regulations.

### Questioned management and consultant costs

We examined \$1,029,838 of services costs charged to HUD funds, and identified \$651,638 (63 percent) as ineligible or inadequately supported. All except \$3,700 of this sample involved non-competitively procured services. See Appendix D for details of these costs by vendor.

Type Services	Costs Examined	Ineligible Costs	Costs Not Adequately Supported
Program Management	\$ 323,475	\$ 137,335	\$ 182,000
Architect and Engineering	451,513		181,816
Consultants	95,491	2,525	36,985
Legal Services	159,359	3,509	107,468
Totals	\$1,029,838	\$ 143,369	\$ 508,269

Program Management – Ineligible costs consisted of the following:

- HWP was paid \$84,136 for managing mass grading work, calculated based on a percentage of construction cost method prohibited by HUD regulation (24 CFR 86.36 (f)(4).) HWP calculated the payment at 5.5 percent of \$1,529,744 paid for mass grading work. This cost was unnecessary and ineligible because the Project paid an architect to manage the grading contract and a testing firm to monitor soil conditions during the grading. The City also paid ADA to manage the overall Project.

The program management contract between ICDC and HWP contained several prohibited provisions for cost plus a percentage of cost compensation (Sections 4.3.2 Infrastructure Development fee; 5.2.2 Development Management fee; and 6.9 Master Developer's development fee.)

- HWP was paid \$28,124 for construction management and related overhead expenses on Block 3A. HWP was an affiliate of the LLC company that owned Block 3A. Thus, HWP was paid fees to manage its affiliate's development. Construction management costs were the responsibility of the property owners. Therefore, this cost was unnecessary and ineligible for HUD funding.
- ADA received \$12,081 of duplicate reimbursements from the City. ADA billed the Section 108 Program \$6,000 for check number 1154 on requisition number 29, and again on requisition 31. ADA billed the Section 108 Program \$6,081 for check number 1492, and also billed the Empowerment Zone on payment requisition number 10.
- ADA was reimbursed \$12,994 for a transaction that was later cancelled and not paid. This consisted of two separate billings for \$8,878 and \$4,116 on requisitions for public works costs.



Inadequately supported management costs included \$182,000 that ICDC paid to HWP or its designated affiliates before executing the program management contract. The payments were made from March 1999 and through September 2000. ICDC did not execute the contract with HWP until November 10, 2000. We could not determine whether these costs were necessary Project related expenditures. Considering ADA's responsibility as the City's sub-recipient, and work performed by architects and other Project consultants, the need for additional Project management before November 2000 was questionable.

Architecture & Engineering - The \$181,816 of inadequately supported costs were for invoices that were referenced to two missing contracts. ADA could not locate the contracts. The invoices alone did not describe the services performed.

Consultants - The ineligible costs of \$2,525 were for two duplicate payments. The \$36,985 of inadequately supported costs was paid to four vendors for which ADA could not locate and provide us with contracts. The invoices alone did not describe the services performed.

Legal Services – Ineligible costs included \$3,319 for organizational costs and \$190 for a duplicate payment. The organizational costs were legal fees related to the operating agreements to establish for-profit affiliates of ICDC and HWP, and the development agreement between ICDC and HWP. Expenditures, such as incorporation fees, organizers or management consultants, attorneys, and accountants, whether or not employees of the organization, in connection with establishment or reorganization of an organization, are unallowable except with the prior approval of the awarding agency (Office of Management and Budget Circular A-122, Attachment B, Section 31.)

The inadequately supported costs included invoices for \$22,672 that contained additional organizational costs. We could not determine specific ineligible amounts because the invoices commingled eligible and ineligible activities in lump-sum billings. Invoices for the remaining \$84,796 of unsupported costs did not provide enough information to show the services were necessary and/or project related.

### Excessive land acquisition costs

ICDC paid \$144,447 more than the appraised value of land without adequate documentation to justify the increased costs.

HUD Handbook 1378, *Tenant Assistance Relocation and Real Property Acquisition*, Chapter 5, Section 5-2, Part I, provides that the purchase price may exceed the just compensation amount (established based on the appraisal) when reasonable efforts to negotiate an agreement have failed and an authorized Agency official approves the administrative settlement as being reasonable, prudent, and in the best interest of the public. The justification must be written and included in the files.

We reviewed 93 of 116 property acquisitions. The settlement statement was missing on 1 property and acquisition files were missing on the remaining 22 properties. ICDC paid more than the appraised value for 50 of the 93 properties. We examined the 50 files for justification of the higher prices paid. When documented, we accepted the highest appraised value assigned to the property based on different appraisal methods (e.g., income, market, and replacement cost.) The files contained adequate documentation justifying higher prices for 33 of the 50 properties. The files did not contain adequate justification for \$144,447 paid in excess of appraised values for the remaining 17 properties.

The excessive purchase prices for the 17 properties ranged from 7 to 123 percent over appraised values. A private developer owned 5 of the 17 properties. ICDC paid 123 percent over appraised value for 3 of the 5 properties and 86 and 20 percent over appraised value on the other two properties. (See Appendix E.)

ICDC attempted to justify excessive payments on some properties by citing high condemnation costs. During a HUD review of acquisition costs in June 2000, ICDC provided HUD with a memo indicating \$14,150 was its representative condemnation cost. We requested that ICDC produce documentation to support this estimate, however, no support was provided. The memo was very general and did not provide sufficient information on the legal services (nature of services, hours, and rates) and other costs to support the estimate. It was apparent that the \$14,150

estimate included legal services for court appeals of Special Master rulings. Under the HUD regulations cited above, we conclude that the costs of potential legal appeals should not be considered unless the Special Master process has failed, and an appeal has been filed or an appeal is documented as likely to occur. In the 17 acquisitions with excessive costs, we saw no evidence that the Special Master process had been completed.

Files for 11 of the 17 acquisitions with excessive prices contained documentation showing an estimated condemnation cost of \$1,500. This cost covered a Special Master court proceeding to settle disagreements over property values, and was adequate justification for paying up to \$1,500 above appraised values. ADA officials, who also represented ICDC, stated that they felt higher prices were justified in order to avoid the time and higher cost of condemnation and to complete the purchases expeditiously. However, higher costs for legal appeals of condemnations and acquisition delays were not documented for 12 properties and were inadequately documented for 5 properties.

#### Missing acquisition records

ICDC could not locate acquisition records for 23 properties. Because of poor accounting records, it was not feasible for us to determine the amounts paid for the 23 properties. Costs for the 23 properties were unsupported and therefore not allowable as costs charged to HUD funds.

ADA and ICDC are required to maintain financial and other records for 3 years from the date of the final expenditure report or until after all litigation, claims, or audit findings started before the expiration of the 3-year period, have been resolved (24 CFR 85.42.)

#### Ineligible relocation claims

The City reimbursed ADA for \$15,132 of ineligible relocation claims made by ICDC. ICDC did not pay \$7,304 in rental assistance to five individuals, and paid \$7,828 to two property owners using an incorrect claim method.

**Relocation Costs Not Paid**

<b>Property Address</b>	<b>Amount Approved</b>	<b>Amount Paid</b>	<b>Amount Not Paid</b>
844 Harwell	\$ 12,090	\$ 9,672	\$ 2,418
36 J. P. Brawley	9,140	6,414	2,726
36 J. P. Brawley	9,565	8,089	1,476
38 Taliaferro	2,268	1,944	324
38 Taliaferro	1,395	1,035	360
Total			\$ 7,304

ICDC issued checks for the \$2,418 and \$324 amounts shown in the table, but the checks never cleared the bank. ICDC later voided the checks. We found no evidence that ICDC wrote checks to the claimants for \$2,726 and \$1,476, and ICDC underpaid one claimant by \$360. Costs that are not incurred are not eligible.

HUD Handbook 1378, Section 3-7, *Additional Rules Governing Replacement Housing Assistance*, provides that rental assistance shall be disbursed in periodic installments. The full amount of the approved payment shall be disbursed, whether or not there is any later change in the person's income or rent, or in the condition or location of the person's housing.

ICDC used an incorrect method to calculate \$7,828 claimed for two individuals. The owners of 844 Harwell and 36 J. P. Brawley filed, and ICDC paid, "Fixed Payment" claims when the owners were only entitled to receive "actual moving and related expenses." ICDC approved and paid \$1,000 and \$6,828 to the respective property owners. Because these were rental properties, the owners were only entitled to receive payment of actual moving and related expenses (49 CFR 24.306 (a), (4) and (5).) The files did not contain documentation of any actual moving costs. Therefore, we could not determine how much the owners were entitled to receive in comparison to what ICDC paid.

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**City of Atlanta  
Comments**

In response to recommendation 2A the City stated:

"Up until the exit conference with the OIG, it has been the City's position that the Integral Group and its team of design consultants, were properly procured in response to a

properly advertised RFP. Based upon the belief that the development team was properly procured, the City Council acted on September 17, 2001, with approval by Mayor Campbell on September 21, 2001, to accept the development team for the Historic Westside Village.

“Unbeknownst to the City until the April 28, 2003 exit conference, a former ADA employee had written the Integral Group rejecting the response to the RFP. The same employee in a later memo to former City Chief Operating Officer Larry Wallace indicated that ADA had selected the Integral Group as its development partner. Despite the conflicting written documentary evidence by the former ADA employee, in reality, both Integral and ADA proceeded as if ADA had accepted the proposal from the Integral Group. The City, likewise, based on the indication it received from ADA, proceeded as if the response to the RFP from the Integral Group had been accepted.

“The City and ADA will make every attempt to provide supporting documentation for those expenditures cited by the OIG as inadequately supported. For expenditures declared to be ineligible or for which supporting documentation cannot be provided the City acknowledges that the Section 108 Program must be reimbursed.

“The City will either provide documentary evidence to support the \$3,700 of legal expenses or reimburse the Section 108 program.”

The City agreed with recommendations 2B and 2D.

Regarding recommendations 2C and 2E, the City stated:

“The acquisitions in question are primarily those paid through ADA’s (or predecessor AEDC’s) administrative policy approved by the Board of Directors of AEDC in 1994. This policy allowed staff to negotiate up to 20% above Fair Market Value with property owners within the Historic Westside Village site. These acquisitions were monitored and approved by HUD during a Compliance Review held in 1996. We understand that it is now the OIG position that these acquisitions were improperly made but feel some allowance should be made as HUD had

previously accepted them. We look forward to further discussions regarding this recommendation.

“The City and ADA apologize for not having the individual acquisition files for these 23 properties available. Due to the reorganization from the Atlanta Economic Development Commission to the Atlanta Development Authority as well as several office moves and staff changes, these files have been disassembled. Progress is being made in relocating and restructuring the files for these properties and will make them available to HUD for review as soon as possible. Again it should be noted that these acquisition files were reviewed and monitored by HUD in December, 1996 and no findings were noted.”

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## OIG Evaluation of City Comments

The City response does not respond directly to recommendation 2A. The City believed ADA had accepted the contract proposal by Integral Group, yet there was no contract between ADA and the Integral Group, and Integral Group did not pay \$2,374,725 for project land as contained in their bid proposal.

HUD requested this audit of the HWV project because its internal review identified questionable expenditures that the City could not support. HUD gave the City ample opportunity to provide support and explanations for questioned expenditures. During this audit, OIG also requested supporting documentation from the City, ADA, and ICDC, providing another opportunity for them to adequately justify expenditures. OIG tested a sample of non-competitive services expenditures and found that 63 percent were ineligible or inadequately supported as to the nature of services received and whether such services were necessary and project related. The balance of service costs, whether tested by OIG or not tested, cannot be deemed reasonable due to the non-competitive procurements. HUD and OIG have found that all of the contracted services paid with \$1.35 million of HUD funds were non-competitively awarded in violation of HUD regulations. Further, inadequate City and ADA accounting records and accounting control deficiencies (duplicate expense claims) preclude further efforts to test or verify expenditures of HUD funds. We conclude that further review of City and

ADA records would be unproductive. The opportunity for the City and ADA to adequately support the questioned expenditures has passed. The City needs to repay \$1.35 million to the Section 108 Program accounts where it will be available for future HWV project costs.

The City agreed with recommendations 2B and 2D, and should provide supporting documentation to HUD or documentation confirming repayment of questioned expenditures.

Recommendations 2C and 2D involve excessive acquisition prices on 17 properties and missing documentation for 23 property acquisitions, respectively. The City is incorrect in its belief that HUD reviewed these acquisitions in 1996. HUD records indicate that only 3 of the 40 properties were previously reviewed. During our audit, no information was provided to us concerning a policy to allow payment of up to 20 percent above appraised value. This policy does not comply with HUD regulations. The City needs to provide adequate support to HUD for the prices paid on the 40 acquisitions, or repay the excessive amounts.

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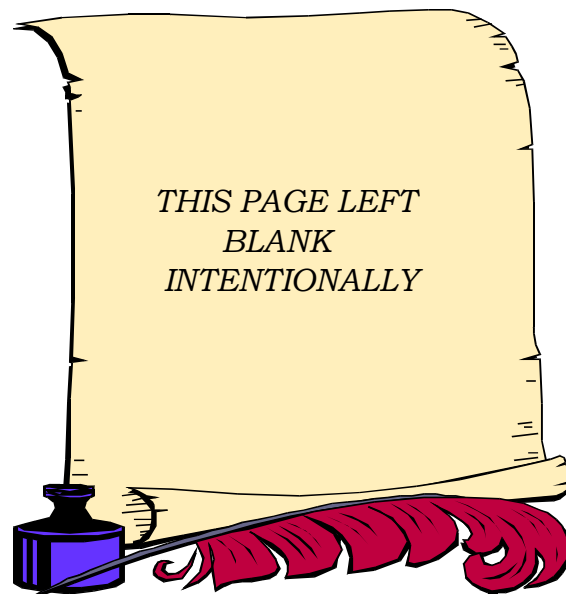
## Recommendations

We recommend that HUD:

- 2A. Require the City to reimburse the Section 108 Program for \$1,350,116 of service costs incurred without competitive procurements.
- 2B. Require the City to provide adequate support for \$3,700 of legal costs (checks 10314 and 1007), or reimburse the Section 108 Program.
- 2C. Require the City to provide adequate support or reimburse the Section 108 Program \$144,447 for excessive land acquisition costs.

- 2D. Require the City to reimburse the Section 108 Program \$15,132 for the ineligible relocation claims. If the City can document subsequent payment of the unpaid amounts and/or the correct claims for actual moving and related expenses of landlord owners, they may reclaim those amounts.
- 2E. Require the City to document the acquisition costs of 23 properties where the files or a settlement statement were missing, or determine amounts paid and reimburse the Section 108 Program. If the City finds the missing documentation, HUD should review it to ensure the purchase prices were justified.





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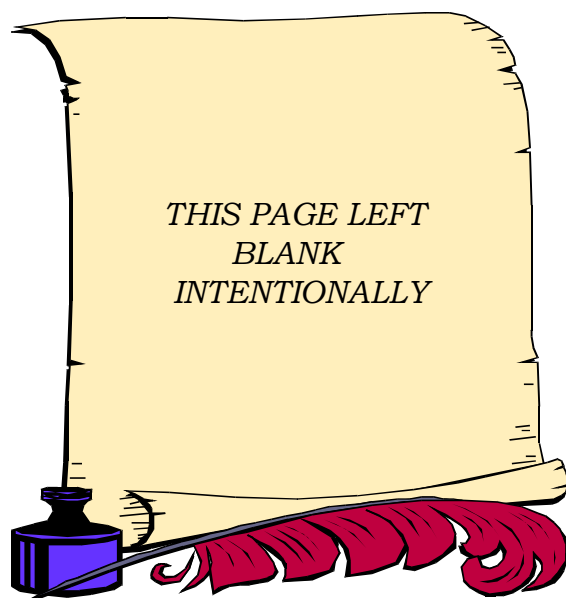
# Management Controls

In planning and performing our audit, we considered management and accounting control systems of the City of Atlanta and ADA to determine our auditing procedures. Our review of management controls was not performed to provide assurance on management controls. Management controls include the plan of organization, and methods and procedures adopted by management to ensure that goals are met. Management controls include the processes for planning, organizing, directing, and controlling Project operations.

We assessed the management controls that we determined to be relevant to our audit objectives, including controls over Project operations; compliance with laws and regulations; and safeguarding resources.

A significant weakness exists if management controls do not give reasonable assurance that the entity's goals and objectives are met; that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained, and fairly disclosed in reports.

Significant weaknesses in the controls we assessed are discussed in Finding 1. Internal control weaknesses were primary causal factors for audit Findings 1 and 2.



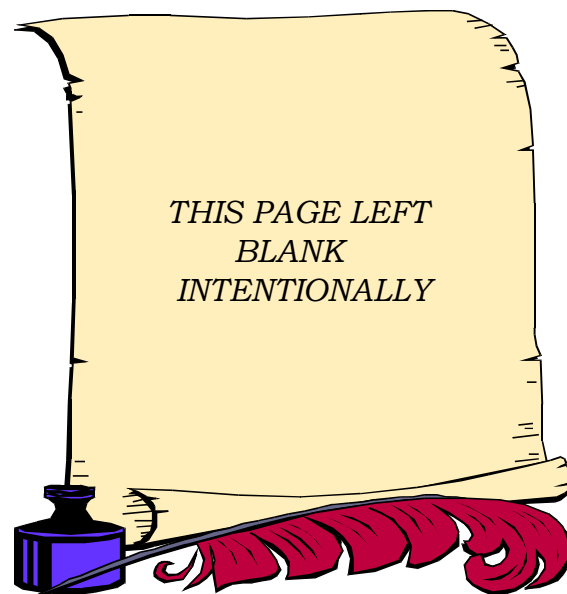
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# Follow-Up On Prior Audits

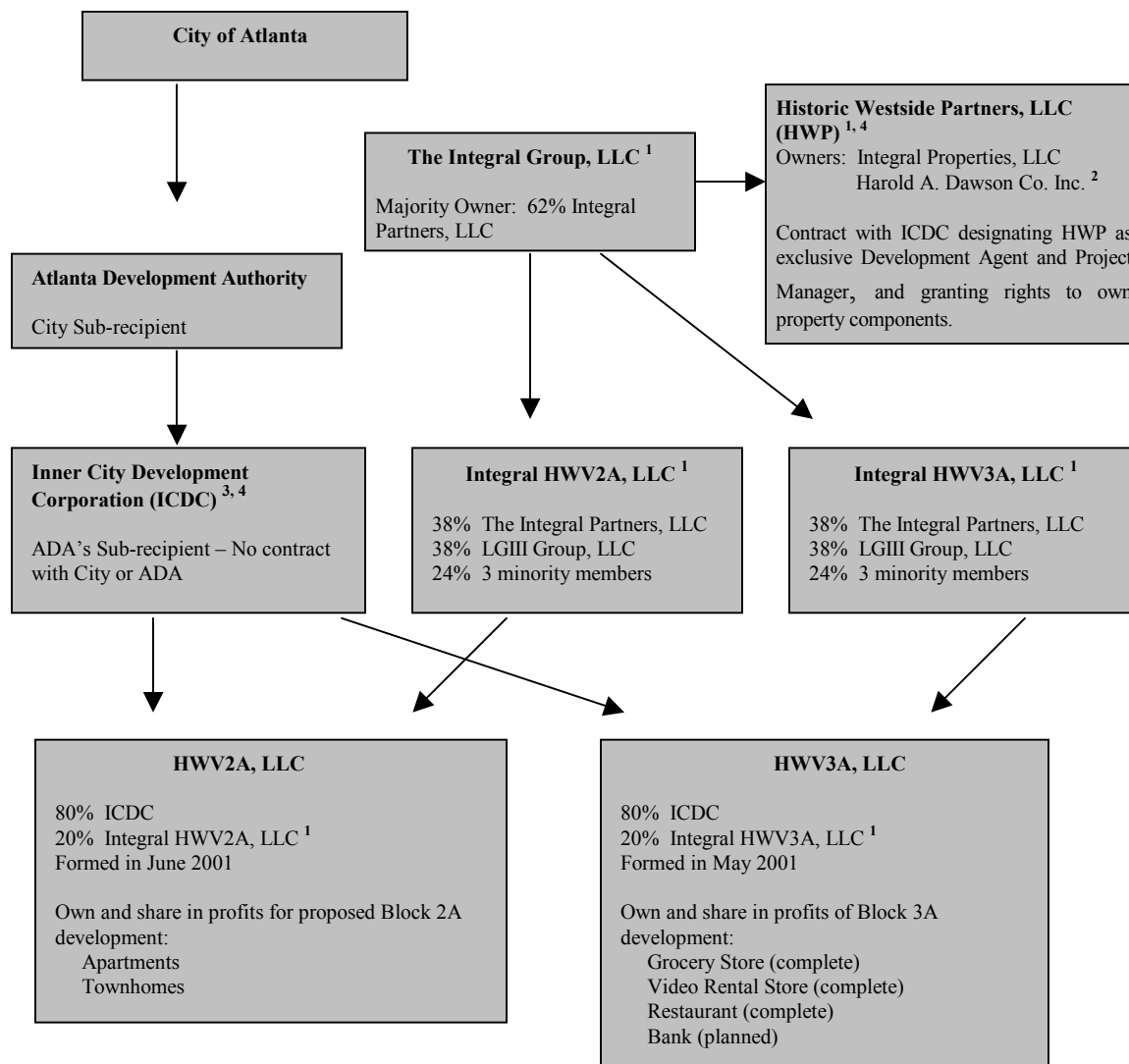
This was the first Office of Inspector General audit on the City's Section 108 Loan and EDI grant for the Historic Westside Village Project.

HUD's CPD division completed a Technical Assistance and Compliance Review of the City's operations in March 2000. The review included, among other programs, the Section 108 Loan and EDI grant for the Historic Westside Village Project. HUD's report contained six findings and two concerns related to the Section 108 Loan Program. The findings and concerns involved issues that we also reviewed and identified further violations as presented in Findings 1 and 2 of this report.

ADA, the City's sub-recipient, obtained annual independent audits of its operations. We reviewed the independent auditor's reports for fiscal years 1999 through 2001. The reports did not contain any findings related to our audit objectives or the issues discussed in Findings 1 and 2.



# Schedule of Affiliated Project Developers



→ Affiliations

<sup>1</sup> These firms all shared a common principal and operated from the same business address.

<sup>2</sup> Resigned from HWP in December 2001.

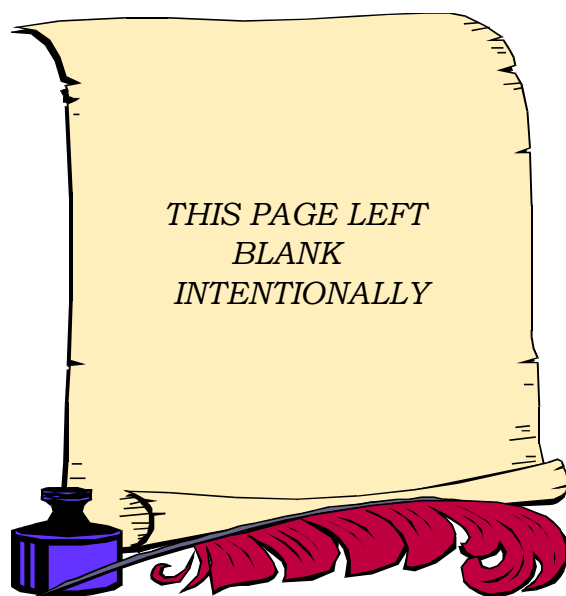
<sup>3</sup> No sub-recipient agreement with the City or ADA. Without sub-recipient authority:

- Received and disbursed program funds,
- Held title to land purchased with program funds,
- Transferred program land to LLCs
- Encumbered project land

<sup>4</sup> Program Management and Development Agreement between ICDC & HWP designated ICDC as Master Developer and HWP as Exclusive Development Agent and Project Manager.

The agreement also preselected the following without competition:

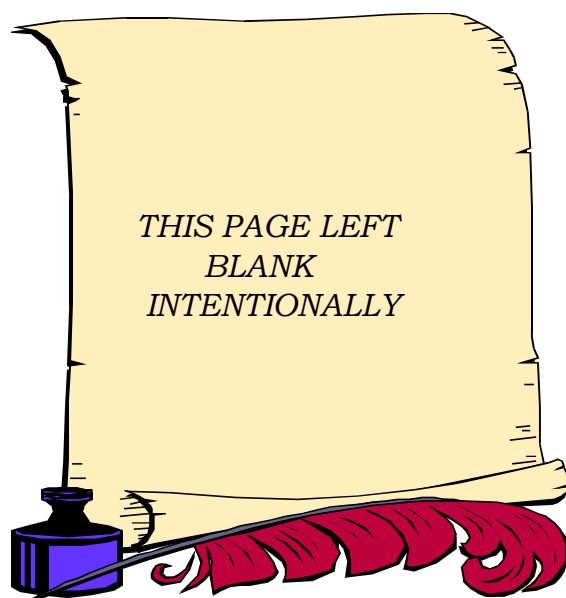
- 2 Exclusive Leasing Agents
- 12 Consultants



# Service Vendors Not Competitively Procured

Vendors	Costs reimbursed By The City	Costs Reimbursed With Section 108 Funds
<b>Program Management</b>		
Harold A. Dawson Company, Inc. <sup>2</sup>	\$ 148,000	\$ 118,000
Historic Westside Partners, LLC <sup>2</sup>	374,178	122,481
Integral Group, LLC <sup>2</sup>	148,000	118,000
The Integral Building Group, LLC	14,676	14,676
Subtotal - Management	684,854	373,157
<b>Architecture &amp; Engineering</b>		
Greenhorn & O' Mara, Inc. <sup>2,3</sup>	22,056	22,056
Altamira Design & Common Sense <sup>3</sup>	393,378	209,345
Turner and Associates <sup>3</sup>	441,564	235,460
Subtotal - A & E	856,998	466,861
<b>Site Work</b>		
Russell Environmental Services, Inc. <sup>3</sup>	343,284	49,659
Subtotal - Site work	343,284	49,659
<b>Consultants</b>		
Grice & Associates, Inc. <sup>2</sup>	16,024	16,024
Haddow & Company <sup>2</sup>	15,571	
Halliday Capital <sup>2</sup>	81,971	
Investments Techniques, LTD. <sup>2</sup>	16,275	16,275
PFK Consulting <sup>2</sup>	7,534	7,534
R & D Test & Drilling, Inc. <sup>2</sup>	20,231	9,346
R & D Environmental	43,890	36,815
CH2MHILL	50,016	50,016
Robert Charles Lesser & Co. <sup>2</sup>	5,455	5,455
Rodgers Prime Consultants <sup>2</sup>	12,360	3,360
Strickland Communication <sup>2</sup>	20,294	20,294
Subtotal - Consultants	289,621	165,119
<b>Legal</b>		
Greenberg & Traurig (formerly Minkin & Snyder) <sup>1</sup>	214,708	205,638
Hunton Williams <sup>1</sup>	46,787	44,808
Sheri Labovitz, P. C. <sup>1</sup>	75,274	44,874
Subtotal - Legal	336,769	295,320
<b>Grand Total</b>	<b>\$ 2,511,526</b>	<b>\$ 1,350,116</b>
<sup>1</sup> These firms provided legal services without any contracts.		
<sup>2</sup> These firms comprised the Development Team and were pre-selected or specifically named as Project contractors in ICDC's Program Management & Development Agreement.		
<sup>3</sup> ADA letter dated October 13, 2000, showed the only solicitation was through undocumented telephone contacts.		



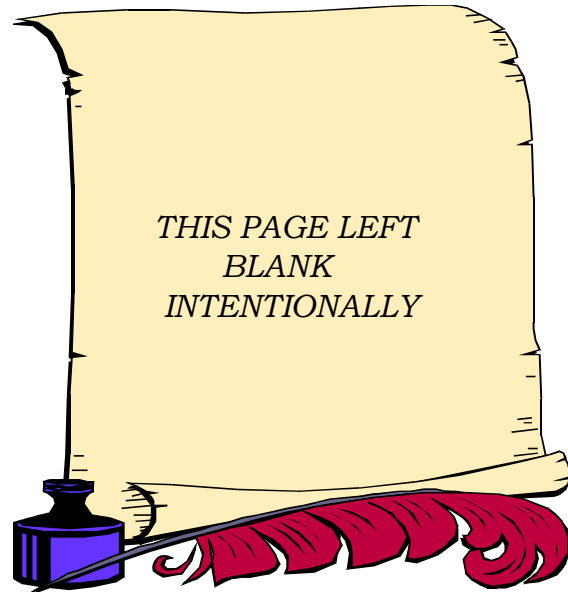


# Summary of Questioned Costs

<u>Recommendation No.</u>	<u>Ineligible<sup>1</sup></u>	<u>Unsupported<sup>2</sup></u>
2A	\$1,350,116	
2B		\$ 3,700
2C		144,447
2D	<u>15,132</u>	<u>          </u>
Totals	<u>\$1,365,248</u>	<u>\$148,147</u>

<sup>1</sup> Ineligible - Costs that are questioned because of an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other document governing the expenditure.

<sup>2</sup> Unsupported - Costs charged to a HUD-funded or insured program or activity whose eligibility cannot be determined at the time of audit since costs were not supported by adequate documentation.



# Ineligible and Unsupported Service Costs

Payee	Check Number	Check Date	Check Amount	Ineligible Costs	Inadequately Supported Costs
<b>Program Management</b>					
Harold A. Dawson Company	1009	3/17/99	\$ 16,667		\$ 16,667
Harold A. Dawson Company	1034	4/22/99	8,333		8,333
The Integral Group, LLC	1010	3/17/99	16,667		16,667
The Integral Group, LLC	1035	4/22/99	8,333		8,333
Harold A. Dawson Company	1081	7/23/99	15,000		15,000
Harold A. Dawson Company	1092	8/27/99	6,000		6,000
Harold A. Dawson Company	1111	10/01/99	6,000		6,000
Harold A. Dawson Company	1124	10/22/99	6,000		6,000
Harold A. Dawson Company	1154	12/21/99	6,000	6,000	
Harold A. Dawson Company	1247	4/18/00	6,000		6,000
Harold A. Dawson Company	1269	5/22/00	6,000		6,000
Harold A. Dawson Company	1309	8/28/00	12,000		12,000
Harold A. Dawson Company	1374	12/22/00	6,000		6,000
The Integral Group, LLC	1082	7/23/99	15,000		15,000
The Integral Group, LLC	1094	8/27/99	6,000		6,000
The Integral Group, LLC	1110	10/1/99	6,000		6,000
The Integral Group, LLC	1123	10/22/99	6,000		6,000
The Integral Group, LLC	1152	12/21/99	6,000		6,000
The Integral Group, LLC	1248	4/18/00	6,000		6,000
The Integral Group, LLC	1268	5/22/00	6,000		6,000
The Integral Group, LLC	1308	8/28/00	12,000		12,000
The Integral Group, LLC	1375	12/22/00	6,000		6,000
Historic Westside Partners	1376	12/22/00	84,136	84,136	
Historic Westside Partners	1492	10/10/01	6,081	6,081	
Historic Westside Partners	No Check	<sup>1</sup>	8,878	8,878	
Historic Westside Partners	No Check	<sup>1</sup>	4,116	4,116	
Historic Westside Partners	1463	8/9/01	6,081	6,081	
Historic Westside Partners	1466	8/28/01	6,105	6,105	
Historic Westside Partners	1482	9/27/01	9,779	9,779	
Historic Westside Partners	1491	10/9/01	6,159	6,159	
<b>Subtotals – Program Management</b>			\$ 319,335	\$ 137,335	\$ 182,000
<b>Architecture &amp; Engineering</b>					
Turner Associates <sup>2</sup>	1051	5/18/99	\$ 50,000		\$ 50,000
Altamira Design & Common Sense <sup>2</sup>	1086	8/05/99	11,060		11,060
Altamira Design & Common Sense	1098	8/31/99	9,493		9,493
Altamira Design & Common Sense	1117	10/31/99	6,209		6,209
Altamira Design & Common Sense	1134	11/09/99	2,960		2,960
Altamira Design & Common Sense	1156	12/21/99	5,618		5,618
Turner Associates	1149	12/21/99	90,224		90,224

# Appendix D

Payee	Check Number	Check Date	Check Amount	Ineligible Costs	Inadequately Supported Costs
Altamira Design & Common Sense	1214	3/21/00	4,075		4,075
Altamira Design & Common Sense	1264	5/03/00	872		872
Altamira Design & Common Sense	1314	8/28/00	1,305		1,305
<b>Subtotals - A&amp;E</b>			\$ 181,816	\$ 0	\$ 181,816
<b>Consultants</b>					
Investment Techniques, LTD. <sup>2</sup>	1089	8/11/99	\$ 2,500		\$ 2,500
R & D Environmental Consultants <sup>2</sup>	1306	8/28/00	7,999		7,999
R & D Testing & Drilling, Inc. <sup>2</sup>	1300	8/16/00	20,513		20,513
Strickland Communications <sup>2</sup>	1053	5/24/99	5,579		5,579
Strickland Communications	1067	6/17/99	394		394
Strickland Communications	1245	4/18/00	1,000	1,000	
Strickland Communications	1274	6/02/00	1,525	1,525	
<b>Subtotals – Consultants</b>			\$ 39,510	\$ 2,525	\$ 36,985
<b>Legal Services</b>					
Minkin & Snyder	1038	5/07/99	\$ 3,741	\$ 1,628	\$ 2,113
Minkin & Snyder	1014	3/22/99	1,993	370	1,623
Battle-URA-Specialists, Inc.	10314	2/19/99	2,500		2,500
Battle-URA-Specialists, Inc.	1007	3/17/99	1,200		1,200
Minkin & Snyder	1071	6/30/99	3,031	740	2,291
Minkin & Snyder	1068	6/21/99	3,809		3,809
Minkin & Snyder	1102	9/01/99	946		946
Greenberg Traurig	1271	5/22/00	18,449	141	18,308
Greenberg Traurig	1218	3/28/00	21,411		21,411
Sheri Labovitz, P.C.	1439	7/20/01	18,017		18,017
Sheri Labovitz, P.C.	1424	6/24/01	13,297		13,297
Sheri Labovitz, P.C.	1423	6/21/01	8,343		8,343
Sheri Labovitz, P.C.	No check	<sup>3</sup>	1,903		1,903
Sheri Labovitz, P.C.	1494	10/12/01	1,269		940
Greenberg Traurig	1432	6/29/01	7,357		7,357
Greenberg Traurig	1502	10/31/01	190	190	
Greenberg Traurig	No check	<sup>3</sup>	3,850	440	3,410
<b>Subtotals - Legal</b>			\$ 111,306	\$ 3,509	\$ 107,468
<b>GRAND TOTALS</b>			\$ 651,967	\$ 143,369	\$ 508,269
<sup>1</sup> Cancelled transactions.					
<sup>2</sup> 6 contracts could not be found.					
<sup>3</sup> No evidence of payment.					

# Excessive Prices Paid for Land

Property Address	Purchase Date	Appraised Value	Purchase Price	Excessive Purchase Price	Excess Percentage
843 Harwell <sup>1</sup>	2/19/96	\$ 6,650	\$14,860	\$ 8,210	123 %
880 Harwell <sup>2</sup>	1/16/96	20,000	26,500	6,500	33 %
882 Harwell <sup>2</sup>	1/16/96	51,226	56,500	5,274	10 %
36 JP Brawley <sup>2</sup>	11/9/95	42,563	50,745	8,182	19 %
852 Mayson Turner <sup>2</sup>	12/14/95	74,722	85,800	11,078	15 %
853 Mayson Turner <sup>1</sup>	2/19/96	14,000	31,285	17,285	123 %
863 Mayson Turner <sup>2</sup>	10/26/95	7,500	9,999	2,499	33 %
843-845 Mayson Turner <sup>1</sup>	2/1/96	40,200	48,380	8,180	20 %
847-849 Mayson Turner <sup>1</sup>	2/19/96	12,300	27,486	15,186	123 %
799 MLK <sup>2</sup>	9/18/95	70,000	75,000	5,000	7 %
839-841 MLK	11/14/95	71,000	95,800	24,800	35 %
55 Raymond <sup>2</sup>	4/15/96	27,500	29,400	1,900	7 %
18 Taliaferro <sup>2</sup>	3/7/96	44,786	52,800	8,014	18 %
22 Taliaferro <sup>1</sup>	2/19/96	20,400	37,989	17,589	86 %
56 Taliaferro <sup>2</sup>	3/7/96	15,000	18,000	3,000	20 %
47&49 Taliaferro (2 properties) <sup>2</sup>	1/26/96	9,150	10,900	1,750	19 %
<b>Total</b>				\$144,447	
<sup>1</sup> 5 properties owned by one person/developer.					
<sup>2</sup> 11 property acquisition files documented expected condemnation costs of \$1,500.					



# City of Atlanta Comments



## CITY OF ATLANTA

SHIRLEY FRANKLIN  
MAYOR

DEPARTMENT OF PLANNING AND COMMUNITY DEVELOPMENT

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CHARLES GRAVES, III  
COMMISSIONER

BUREAU OF HOUSING  
AND CODE COMPLIANCE  
PHILIP E. SMITH, DIRECTOR

May 19, 2003

Ms. Nancy H. Cooper  
Regional Inspector General for Audit  
U. S. Department of Housing and Urban Development  
Region 4, Office of the Inspector General  
Office of Audit, Box 42  
Richard B. Russell Building  
75 Spring Street, SW, Room 330  
Atlanta, GA 30303-3388

**RE: Review of the MLK/Ashby Street Section 108 Loan Program  
Historic Westside Village  
Atlanta, GA**

Dear Ms. Cooper:

Thank you for the opportunity to review the draft report of the audit of the Historic Westside Village project. It is our understanding that the recommendations of the draft are not final and may be modified to some extent by this response. We also appreciated the opportunity to discuss the draft report at an exit conference, held April 28, 2003, with Terry Cover, Narcell Stamps, Nicole Jackson, and Robert Burgess of your staff and John Perry, Stella Taylor and Russell Douglas of the Georgia Office of Community Planning and Development.

Before responding we wish to acknowledge the professionalism and courtesy of your staff, particularly Mr. Stamps, Ms. Jackson and Mr. Burgess in the conducting and preparation of the audit report.

### General Comments

The City of Atlanta has attempted to support the redevelopment of the land lying at the corner of Martin Luther King, Jr. Drive and Joseph Lowery Drive (formerly Ashby Street) for more than 25 years. The property is ideally located next to the Atlanta University complex consisting of several prominent African-American colleges. It is also located in a neighborhood of sensitive and often competing political interests. Part of the difficulty in implementing this project is that from a development standpoint, the private sector has viewed the site with caution, being located in a lower income, high crime area. The award of Section 108 Loan in 1994 gave the project a significant boost but still did not result in a project as the first developer chosen, H. J. Russell Company, left the project in 1998.



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In 1997, former Mayor Bill Campbell reorganized a number of economic development and housing agencies into the Atlanta Development Authority (ADA). With the withdrawal of the H.J. Russell Company from the MLK/Ashby project, the newly organized agency was charged with finding another developer for the project. After a Request for Proposal resulted in only one proposal, ADA chose to become the master developer along with the Integral Group and its design team who were respondents from the RFP. ADA's concept for the development was a mixed use development that became known as the Historic Westside Village, a project hailed by former Mayor Campbell as the largest development in a traditionally African-American community in Atlanta's history.

The Historic Westside Village is to provide an important commercial center for the neighborhood and currently boasts one of the few in-town grocers in the inner city. Additionally it will provide commercial and supporting services to an area where more than one-half billion dollars in investment is planned. HUD funded projects at Magnolia Park, the Villages at Castleberry Hill, the HOPE VI redevelopment of Harris Homes, grants under the Historic Black Colleges and Universities program and years of CDBG/HOME investments in the Vine City neighborhood are all complemented by and will benefit from the Historic Westside Village.

While in hindsight some of the decisions made in the development of Historic Westside Village may be questioned, both City and ADA staff were under intense pressure from the former Mayor and from neighborhood residents to implement the project. The HWV project remains a difficult and complex project to develop and finance. Its future success is highly dependent upon continuing with the project in a timely manner. Should the project not move forward, current lease agreements with the Publix grocery would allow it to close its doors costing the project its anchor tenant. Should Publix close, the impact would likely cost the development its other leases, cost the project its momentum and effectively kill the entire project. The impact would extend much further than the loss of the project. The Atlanta Development Authority guaranteed a \$4,000,000 loan for Phase 3A and as such would suffer grave financial consequences. As the City's redevelopment agency, this would hamper ADA's ability to finance future housing and economic development activities. Accordingly, the City of Atlanta hopes it can still enjoy the help and cooperation of HUD as it addresses the program deficiencies identified by the Inspector General and continue to move the project forward in an expedient manner.

**Finding 1 – Inadequate City and ADA Management and Control of Project Development**

***The City of Atlanta and its sub-recipient, ADA, did not adequately manage and control the Project and \$7,208,000 of HUD funding. The City lost control of the Project and allowed significant violations of HUD requirements to occur without early detection or prompt corrective action.***

***OIG Recommendation 1A: Initiate administrative sanctions against officials of the City, ADA, and ICDC who allowed violations to occur. This should include consideration of limited denials of participation and debarments.***

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**Response:**

The City and ADA are concerned about the findings of the Office of Inspector General regarding the actions of former officials. However, without further information regarding the nature and implications of what administrative sanctions HUD may impose, we must reserve comment. We would however, request that the City be given further clarification on HUD's likely actions prior to public release.

***OIG Recommendation 1B: Before future Community Development Block Grant funding is provided to the City and ADA, require evidence of 1) adequate accounting systems and procedures, 2) adequate procurements systems and controls, 3) controls to monitor compliance with Federal funding requirements, and 4) adequate City and Board oversight of ADA. HUD should monitor procurements and Board minutes during Project planning and development until the City and ADA have demonstrated compliance.***

**Response:**

The City of Atlanta and the Atlanta Development Authority are in basic agreement with the OIG assessment that tighter accounting procedures, systems and controls are needed in regards to the HWV project and welcomes increased HUD monitoring of the project.

The City disagrees that future Community Development Block Grant funding be withheld from the City as it believes its already has adequate accounting systems, procurement controls and monitoring systems with regards to its CDBG projects. The audit examined only one Section 108 project, which involved unique development challenges, many funding sources and multiple partnerships. The HWV project remains distinctive from the City's annual CDBG grant processes.

The City's annual CDBG grant is mostly allocated to small service projects for a variety of social services, housing projects benefiting individual homeowners, and some infrastructure projects implemented by City departments. Over the years, the City has demonstrated its capacity to carry out these grant-funded activities in accordance with federal administrative standards. For the past several monitoring reviews by HUD, the City's accounting procedures and the procurement system have been found in compliance without any findings. The City has established prerequisites for applying for CDBG so that all subrecipients must submit audits and financial statements, financial management procedures, evidence of corporate status and licensure, and demonstrated experience and success in related activities before the City even considers providing any CDBG funding. Subrecipient agreements have been strengthened, all monitoring/reporting requirements are contractually required, and efforts continue to reimburse for only allowable and eligible items in approved contracts. The City's grants management and grants accounting units impose independent reviews of contracts and reimbursements apart from the City's implementing agencies that carry out contract administration. Based on this, the City respectfully requests that resolution of the audit of the HWV Section 108 project not be tied

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to receipt of future CDBG funding since HUD has found that adequate controls have been in effect for annual grant activities.

With respect to the HWV project, the City has taken the following actions to ensure improved control, oversight, and monitoring controls of the HWV project:

- City staff will conduct monthly monitoring visits of ADA for the next six months and quarterly thereafter subject to satisfactory compliance in the first six months.
- City and ADA staff are conducting weekly HWV project meetings to discuss project progress, compliance issues, procurement, and other concerns related to recapture of program income, needed contracts and agreements, etc. These meetings have greatly improved communication between the City and ADA and are helping to prevent further violations of HUD regulations.
- City and ADA HWV project staffs are conducting monthly meetings with Mayor Franklin to receive project guidance and discuss needed action from the ADA Board of Directors prior to the Board meeting. This meeting has resulted in increased understanding and oversight of the project from the ADA and ICDC Board of Directors.
- The City Internal Auditor has established an external audit monitoring function headed by an audit manager experienced in project accounting and financial reporting. This function will monitor all external audits conducted on city activities and programs, review audit reports and the city's responses, and monitor implementation of audit recommendations. The emphasis of this function is on audits by state and federal grantors and on the Single Audit conducted by the city's external financial auditor. The Audit Committee and Internal Auditor will report annually to the Mayor and City Council on the status of uncorrected findings and implementation of recommendations. These activities, required by the City Charter and Code of Ordinances, will provide added assurance that the improved controls and compliance pledged in this response are in fact carried out.

The Atlanta Development Authority has also taken major steps in addressing its accounting procedures, procurement policies and managerial oversight of the Historic Westside Village project. As a sub-agency of ADA, ICDC will adopt ADA's revised policies. Highlights of ADA actions are presented below. A more complete list of improvements and actions taken may be found in a letter from Interim President Ernestine Garey to Commissioner Charles Graves, dated May 19, 2003 and attached as Exhibit A.

- Approved agreement establishing a contractual relationship with ICDC to serve as Master Developer for the Historic Westside Village project. New directors have been appointed to ICDC with Mayor Franklin serving as Chair.

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- Engaged two CPA firms to restructure and audit ICDC's financial records.
- ADA has restructured its financial organization for enhanced control over procurement, budget approvals and accounting checkpoints. Appointed a Project Compliance Coordinator to focus on HUD compliance issues related to the Historic Westside Village project.
- ADA's Chief Finance Officer or designee and Project Compliance Coordinator will approve all procurements, contracts and development agreements before execution to ensure proper budgeting and compliance with federal regulations. This reflects a positive change from the previous system whereby the Project Manager for Historic Westside Village approved all procurements, contracts and expenditures. During interim monitoring period indicated above, the City will also approve procurements paid for federal funds.

***OIG Recommendation 1C: Remove ICDC as a Project participant and prohibit it from expending any HUD funds under the project management and development contract with HWP.***

**Response:**

The City of Atlanta and ADA respectfully disagree with this recommendation, at least in respect to the development of Parcels 3A, 2A and 3C. As indicated above, delays in the project may result in the loss of Publix as an anchor tenant. The removal of ICDC from the project would basically unwind all progress to date and force the City and ADA to start the project over. This of course would cause great delay; void the private financing already obtained for these phases and effectively kill the project.

Alternatively, the City proposes that ICDC be allowed to remain in the project for Phase 3A, 2A and 3C and that the City and ADA will prepare a Request for Proposals prior to the commencement of any subsequent phases.

The City and ADA have already remedied many of the deficiencies the OIG found with ICDC by the following actions:

- Executed a contractual agreement between ADA and ICDC.
- Elected new officers for ICDC with the members of the ADA Board of Directors also serving as the ICDC Board of Directors. Mayor Franklin serves as Chair of both Boards. Management oversight of ICDC activities will be provided by the ADA Board.
- ADA has engaged two independent CPA firms to restructure and audit ICDC's financial records.

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***OIG Recommendation 1D: Recover ownership of Project land or appropriate program income from the transferred lands to repay the Section 108 loan or, with written HUD approval, for future project development, This includes the \$1.7 million ICDC should have collected for Block 2A.***

**Response:**

The City's Section 108 funds have been utilized, in part, to purchase approximately 16 acres as the site for the development of Historic Westside Village. As originally contemplated, the funds utilized for acquisition would have been recovered by the sale of the site to a private developer. Upon ADA becoming the master developer in 1998, the project was changed to utilize the land as ADA's contribution to the project and as collateral to secure private financing to complete the project. City staff was requested by the former Mayor and the former ADA President to restructure the project so that any program income generated to repay the Section 108 loan would be derived from cash flow from the project as opposed to land sales.

The City and ADA understand the OIG's position that the land for Blocks 3A and 2A have been transferred to for-profit limited liability corporations, HWV3A, LLC and HWV2A, LLC respectively. However, ICDC, ADA's wholly owned subsidiary holds a 99.99% interest in HWV3A and a 25% interest in HWV2A. As indicated above, the land represents ADA's "equity" investment that allows ICDC this ownership position in the HWV3A and HWV2A phases and is used to secure private financing in the project.

The City and ADA agrees with the OIG that the City should have received compensation when the land was transferred to the two limited liability corporations. However, to accept OIG recommendation to recover ownership appropriate income for Block 3A is not practical without risking the loss of the anchor tenant and the entire project. The private financing would have to be paid or collateralized from another source not currently available to either ADA or the City. Greater flexibility is available for Block 2A as construction has not yet begun. As such the City and ADA propose the following:

- The City of Atlanta will amend the Section 108 program to reflect the project change. The authorization to amend the Section 108 program has been approved by the Atlanta City Council and is awaiting submission to HUD. The Section 108 program will need to be further amended pending final resolution of this audit as to any program costs that may be disallowed.
- The ADA and ICDC will amend its partnership agreement for Block 3A. Cash flow generated from Block 3A will be divided between the City and ICDC in a 60% and 40% split respectively. The HWV3A LLC, and the ADA and ICDC Board of Directors have approved this sharing of cash flow. The agreement will be presented to the Atlanta City Council for approval within 45 days of acceptance of the proposal by HUD.

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- Block 2A is still in the planning and predevelopment stage. ICDC and Integral HWV2A, LLC executed an Operating Agreement for HWV 2A, LLC ("HWV 2A") on June 1, 2001. In order to facilitate the development of Block 2A, ICDC transferred the land to HWV 2A at that time. The HWV 2A Operating Agreement required HWV 2A to pay \$1,700,000 for the land acquisition. After the reconstruction of the general ledger and an independent audit to determine the actual cost of the Block 2A parcel, this provision of the Operating Agreement will be amended to reflect the true acquisition cost of the land. HWV 2A will then repay the actual acquisition cost of this parcel to the City as program income. In the event the land acquisition cost cannot be repaid in full, the ICDC Board of Directors has approved a resolution allotting 25% of the net cash flow from the development of the Block 2A parcel to the City as program income.
- For all future phases of the Historic Westside Village project, the City will take all steps necessary to record and receive appropriate program income from each phase of the project.

***OIG Recommendation 1E: Require ADA and/or ICDC to contribute the \$1.7 million ICDC agreed to contribute to the Block 3A component, and seek to remove the related encumbrance of Block 1.***

**Response:**

The City and ADA disagree with the OIG's premise and recommendation. ICDC has in fact contributed the amount of \$1,990,000 in funds from the Tax Allocation District. Further the Urban Residential Finance Authority has guaranteed a private loan in the amount of \$4,000,000. Any confusion surrounding this contribution was caused by the delay in tax allocation district (TAD) funding to the project. Because of this delay ADA and ICDC were forced to undergo a series of financial maneuverings to keep the project on track. This maneuverings involved borrowing and repaying several sources of funds finally to be taken out by the TAD contribution. To provide further clarification the development agreement for HWV3A, LLC has been amended to remove reference to the required \$1.7 million contribution.

The City does agree that the encumbrance of Block 1 for the Block 3A project was inappropriate and should be removed. Whether or not it is feasible to remove this encumbrance is subject to negotiation with the bank providing the private financing for Block 3A. The City and ADA will explore its options with the bank immediately.

***OIG Recommendation 1F: Require ICDC and ADA respectively, to record the \$72,641 lease termination fee and \$93,968 developer fees as project revenue, and Section 108 program income in accordance with HUD regulations. Require program income to be transferred to the Section 108 project cash account.***

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**Response:**

The City of Atlanta and ADA agree with this recommendation and will transfer the referenced program income to the Section 108 project cash account as soon as the audit of ICDC, verifying this amounts, is completed.

**Finding 2 – The City and ADA Did Not Effectively Control Project Expenditures**

***The City and ADA did not effectively control Project expenditures to ensure they were eligible, reasonable, necessary and supported.***

***OIG Recommendation 2A: Require the City to reimburse the Section 108 Program for \$1,350,116 of service costs incurred without competitive procurements. That amount included \$143,369 of service costs found to be ineligible and \$504,569 found to be inadequately supported to show the costs were eligible, necessary and project related.***

**Response:**

In May 1998, ADA, under its agreement with the City of Atlanta, issued a Request for Proposals for the development of Historic Westside Village. ADA received one response, from the Integral Group, to the properly advertised RFP. In the response, Integral was to serve as project lead but also included in the response as the development and design team a number of other design and marketing consultants including Turner Associates, Altimira Land Planners, Common Sense, Inc., and CB-Richard Ellis. ADA's review of Integral's response found it to be smaller in scope than the project vision provided for in the RFP. At this point, ADA decided to work with the Integral team as the master developer. ADA also added the development firm of Harold Dawson to provide greater strength in the area of commercial development, in particular related to grocery stores. The Harold Dawson Company later removed itself from the project team.

Up until the exit conference with the OIG, it has been the City's position that the Integral Group and its team of design consultants, were properly procured in response to a properly advertised RFP. Based upon the belief that the development team was properly procured, the City Council acted on September 17, 2001, with approval by Mayor Campbell on September 21, 2001, to accept the development team for the Historic Westside Village.

Unbeknownst to the City until the April 28, 2003 exit conference, a former ADA employee had written the Integral Group rejecting the response to the RFP. The same employee in a later memo to former City Chief Operating Officer Larry Wallace indicated that ADA had selected the Integral Group as its development partner. Despite the conflicting written documentary evidence by the former ADA employee, in reality, both Integral and ADA proceeded as if ADA had accepted the proposal from the Integral Group. The City, likewise, based on the indication it received from ADA, proceeded as if the response to the RFP from the Integral Group had been accepted.

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The City acknowledges that the documents rejecting the Integral Group are extremely damaging to ADA's and the City's position that the Integral Group and its design team were properly procured. We would request consideration however, inasmuch as all parties proceeded as if the response to the RFP had been accepted and the written documentation provided by ADA to the City indicates acceptance of the response, the Integral Group and its team members was indeed accepted, that some portion of the procurement process could be approved.

As the major finding from the OIG report, the City looks forward to further discussions of this issue. The City and ADA will make every attempt to provide supporting documentation for those expenditures cited by the OIG as inadequately supported. For expenditures declared to be ineligible or for which supporting documentation cannot be provided the City acknowledges that the Section 108 Program must be reimbursed.

***OIG Recommendation 2B: Require the City to provide adequate support for \$3,700 of legal costs (checks 10314 and 1007), or reimburse the Section 108 Program.***

**Response:**

The City will either provide documentary evidence to support the \$3,700 of legal expenses or reimburse the Section 108 program.

***OIG Recommendation 2C: Require the City to provide adequate support or reimburse the Section 108 Program \$144,447 for excessive land acquisition costs.***

**Response:**

The acquisitions in question are primarily those paid through ADA's (or predecessor AEDC's) administrative policy approved by the Board of Directors of AEDC in 1994. This policy allowed staff to negotiate up to 20% above Fair Market Value with property owners within the Historic Westside Village site. These acquisitions were monitored and approved by HUD during a Compliance Review held in 1996. We understand that it is now the OIG position that these acquisitions were improperly made but feel some allowance should be made as HUD had previously accepted them. We look forward to further discussions regarding this recommendation.

***OIG Recommendation 2D: Require the City to reimburse the Section 108 Program for \$7,304 for relocation costs not paid to claimants and \$7,828 of relocation paid on an ineligible basis. If the City can document subsequent payment of the unpaid amounts and/or the correct claim amount for actual moving and related expenses of landlord owners, they may reclaim those amounts.***



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**Response:**

Based on recent research the City agrees with the OIG that the \$7,304 in relocation payments have not been made and ADA will return these funds to the City for proper handling. The costs identified by ADA as ineligible are still being researched and will either be documented or repaid.

***OIG Recommendation 2E: Require the City to document the acquisition costs of 23 properties where the files or a settlement statement were missing or determine amounts paid and reimburse the Section 108 program. If the City finds the missing documentation, HUD should review it to ensure the purchase prices were justified.***

**Response:**

The City and ADA apologize for not having the individual acquisition files for these 23 properties available. Due to the reorganization from the Atlanta Economic Development Commission to the Atlanta Development Authority as well as several office moves and staff changes, these files have been disassembled. Progress is being made in relocating and restructuring the files for these properties and will make them available to HUD for review as soon as possible. Again it should be noted that these acquisition files were reviewed and monitored by HUD in December, 1996 and no findings were noted.

In summary, the City and ADA accepts the recommendations of the audit report as indicated in our responses above and we look forward to working with the Georgia Office of Community Planning and Development to resolve the outstanding issues.

Again, thank you for your courtesy and professionalism.

Sincerely,



Charles C. Graves, III, Commissioner  
Planning and Development

cc: Mayor Shirley Franklin  
Lynnette Young  
Richard Anderson  
Leslie Ward  
Linda DiSantis  
Ernestine Garey

John Perry  
Narcell Stamps  
Stella Taylor  
Philip Smith  
Jocelyn Ross