
AUDIT REPORT



CITY OF MINNEAPOLIS EMPOWERMENT ZONE PROGRAM

MINNEAPOLIS, MINNESOTA

2003-CH-1007

JANUARY 3, 2003

OFFICE OF AUDIT, REGION V
CHICAGO, ILLINOIS



Issue Date	January 3, 2003
Audit Case Number	2003-CH-1007

TO: Pamela Glekas-Spring, Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative, DEEZ

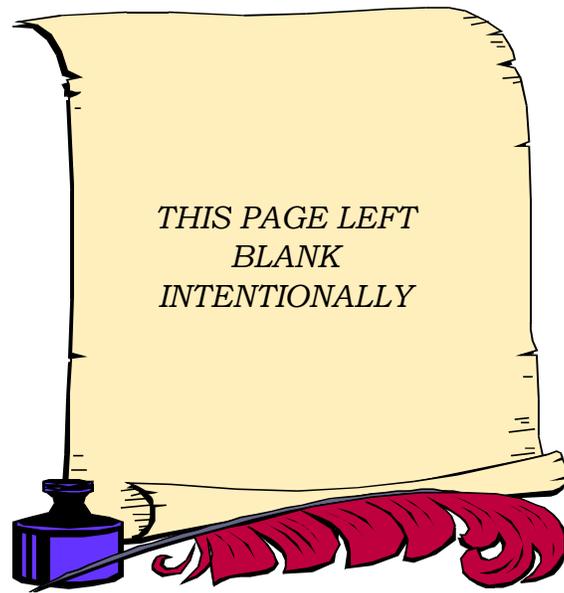

FROM: Heath Wolfe, Regional Inspector General for Audit, Region V

SUBJECT: City of Minneapolis
Empowerment Zone Program
Minneapolis, Minnesota

We completed an audit of the City of Minneapolis' Empowerment Zone Program. The audit was conducted based upon our survey results and requests from Congress. The objectives of our audit were to determine whether the City: (1) efficiently and effectively used Empowerment Zone funds; and (2) accurately reported the accomplishments of its Empowerment Zone Program to HUD. The audit was part of our Fiscal Year 2002 Annual Audit Plan. The audit resulted in three findings.

In accordance with HUD Handbook 2000.06 REV-3, within 60 days please provide us, for each recommendation without a management decision, 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 or your staff have any questions, please contact Edward Kim, Assistant Regional Inspector General for Audit, at (614) 469-5737 extension 8306 or me at (312) 353-7832.

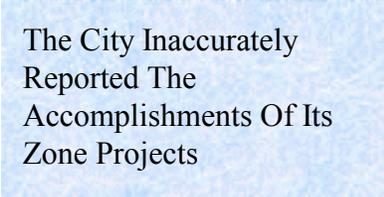


Executive Summary

We completed an audit of the City of Minneapolis' Empowerment Zone Program. The objectives of our audit were to determine whether the City: (1) efficiently and effectively used Empowerment Zone funds; and (2) accurately reported the accomplishments of its Empowerment Zone Program to HUD. The audit was part of our Fiscal Year 2002 Annual Audit Plan. The audit was conducted based upon our survey results and two requests from Congress.

The United States House of Representatives' Conference Report 107-272 directed HUD's Office of Inspector General to review the use of Empowerment Zone funds and to report our findings to the Senate Appropriations Committee. The United States Senate's Report 107-43 also requested us to review the use of Zone funds and report our audit results to Congress.

We concluded that the City did not accurately report the accomplishments of its Empowerment Zone Program to HUD and needs to improve its oversight of Empowerment Zone funds. Specifically, the accomplishments of the City's Empowerment Zone projects were inaccurately reported to HUD and the City inappropriately used \$9,705 of Empowerment Zone funds to pay expenses not related to its Near North Planning and Development project. We also found that the City used Empowerment Zone monies to fund seven projects that have not provided benefits to Empowerment Zone residents or benefited only 3 to 38 percent of Zone residents as of June 2002. Five of the seven projects are scheduled for completion between December 2003 and December 2011, and the remaining two projects were completed between December 2001 and July 2002.



The City Inaccurately Reported The Accomplishments Of Its Zone Projects

As previously mentioned, the City of Minneapolis incorrectly reported the actual status and/or progress for seven of the 10 projects (70 percent) we reviewed from its June 30, 2001 or June 30, 2002 Annual Reports. The City's June 2001 Report contained inaccuracies related to three projects' progress on projected outputs and one project's percentage of completion on project milestones. The City's June 2002 Report contained inaccuracies related to two projects' progress on projected outputs and one project's source of funding. The problems occurred because the City: did not verify the accuracy of the information provided by the projects' administering entities; lacked adequate controls and oversight to assure the reliability of information reported in its Reports to HUD; or failed to verify the accuracy of information included in its Reports.

The City Provided Zone Funds To Projects That Have Not Benefited Zone Residents Or Benefited Between 3 And 38 Percent Of Zone Residents

The City used all of its \$1,825,000 in Empowerment Zone monies committed to fund seven projects that have not benefited Empowerment Zone residents or benefited only 3 to 38 percent of Zone residents as of June 2002. Five of the seven projects are scheduled for completion between December 2003 and December 2011, and the remaining two projects were completed between December 2001 and July 2002. Since the five projects spent all of their Zone funds committed, benefits to Empowerment Zone residents would be expected. However, this has not occurred.

The problem occurred because the City did not ensure that its Empowerment Zone contracts required projects to primarily benefit Zone residents. We believe the City's use of Empowerment Zone funds for the seven projects does not meet HUD's Empowerment Zone regulation at 24 CFR Part 598.215(b)(4)(i)(D) that incorporates the Appendix from the April 16, 1998 Federal Register requiring all projects financed in whole or in part with Zone funds be structured to primarily benefit Zone residents. However, HUD must make a determination whether the City's use of Zone funds was appropriate.

Controls Over Empowerment Zone Funds Need To Be Improved

The City needs to improve its oversight of Empowerment Zone funds. One of the 10 projects we reviewed inappropriately used \$9,705 of Zone funds to pay expenses not related to the Near North Planning and Development project. Since the City spent over \$3.6 million in Empowerment Zone funds as of May 2002 for the 10 projects, the City's inappropriate use of Zone funds was not a systematic break down in its controls over the Empowerment Zone Program. The problem occurred because the City did not adequately monitor the Near North Planning and Development project to ensure the use of Empowerment Zone funds was appropriate.

Recommendations

We recommend that HUD's Director of Renewal Communities/Enterprise Zones/Enterprise Communities Initiative assure that the City of Minneapolis reimburses its Near North Planning and Development project from Empowerment Zone Administration funds for the inappropriate use of Zone funds and implements controls to correct the weaknesses cited in this report.

We presented our draft audit report to the Director of the City of Minneapolis' Empowerment Zone and HUD's staff during the audit. We held an exit conference with the City's Director on December 19, 2002. The City disagreed that Empowerment Zone funds were inappropriately used, but agreed to implement procedures and controls to improve the reporting of information to HUD and ensure that Empowerment Zone contracts meet Empowerment Zone Program requirements regarding benefits to Zone residents.

We included paraphrased excerpts of the City of Minneapolis' comments with each finding (see Findings 1, 2, and 3) and the summary of Empowerment Zone projects reviewed (see Appendix B). The complete text of the comments is in Appendix C with the exception of nine attachments that were not necessary for understanding the comments. A complete copy of the City of Minneapolis' comments with the attachments was provided to HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative.



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Introduction

The City of Minneapolis was designated as an urban Empowerment Zone effective January 1, 1999. The objective of the Empowerment Zone Program is to rebuild communities in poverty stricken inner cities and rural areas by developing and implementing strategic plans. The plans are required to be based upon the following four principles: (1) creating economic opportunity for Empowerment Zone residents; (2) creating sustainable community development; (3) building broad participation among community-based partners; and (4) describing a strategic vision for change in the community.

The Omnibus Budget Reconciliation Act of 1993 authorized the Empowerment Zone Program. The Reconciliation Act provided funding for the Empowerment Zone Program under Title 20 of the Social Security Act. The Program was initially designed to provide \$250 million in tax benefits with \$100 million of Social Service Block Grant funds from the Department of Health and Human Services. The Taxpayer Relief Act of 1997 authorized the Secretary of HUD to designate 15 additional urban areas as Empowerment Zones. The 15 additional urban Empowerment Zones were eligible to share in HUD grants and tax-exempt bonding authority to finance revitalization and job creation over the next 10 years. As of April 30, 2002, the City of Minneapolis drew down and spent \$4,366,557 in Empowerment Zone funds.

The City of Minneapolis is a municipal corporation that is governed by a mayor and a city council. The City's fiscal year is January 1 through December 31. The City's Mayor is the Honorable R.T. Rybak. The Director of the City's Empowerment Zone is Kim W. Havey. The City's books and records for its Empowerment Zone Program are located at 350 South 5th Street, Minneapolis, Minnesota.

Audit Objectives

The objectives of our audit were to determine whether the City: (1) efficiently and effectively used Empowerment Zone funds; and (2) accurately reported the accomplishments of its Empowerment Zone Program to HUD.

Audit Scope And Methodology

We performed our on-site work between June and October 2002. To determine whether the City efficiently and effectively used Empowerment Zone funds and accurately reported the accomplishments of its Empowerment Zone Program, we interviewed staff from: HUD; the City; and administering entities of the City's Zone projects. Based upon the projects' reported expenditures as of April 30, 2002, we selected 10 of the City's 20 projects reported in its June 30, 2001 or June 30, 2002 Annual Reports. The following table shows the 10 projects reviewed.

<i>Project</i>
1. Plymouth Christian Youth Center
2. Minneapolis Public School Wireless Technology
3. Agape 24-Hour Child Development Center
4. Green Institute
5. Near North Phase 1B
6. Park Plaza
7. Near North Planning and Development
8. Coliseum
9. Hawthorne Homesteading
10. Opportunity Kitchen

To evaluate the City's Empowerment Zone Program, we reviewed files and records maintained by: the City; HUD; and the administering entities. We also reviewed: 24 CFR Part 598; the April 16, 1998 Federal Register; HUD's guidance and instructions for the Program; the City's June 2001 and June 2002 Annual Reports; the City's agreements and contracts; approved payment requests related to the projects; and the administering entities' voucher payments, monitoring files, and supporting documentation. We visited or met with representatives for each of the administering entities for the 10 projects included in our audit to review their documentation, reports, and correspondence.

The audit period covered the period January 1, 1999 to April 30, 2002. This period was adjusted as necessary. We conducted our audit in accordance with Generally Accepted Government Auditing Standards.

We provided a copy of this report to the City's Mayor and copies to its Director of the Empowerment Zone.

The City Inaccurately Reported The Accomplishments Of Its Empowerment Zone Projects

The City of Minneapolis incorrectly reported the actual status and/or progress for seven of the 10 projects (70 percent) we reviewed from its June 30, 2001 or June 30, 2002 Annual Reports. The City's June 2001 Report contained inaccuracies related to three projects' progress on projected outputs and one project's percentage of completion on project milestones. The City's June 2002 Report contained inaccuracies regarding two projects' progress on projected outputs and one project's source of funding. The problems occurred because the City failed to maintain adequate controls over its Annual Reports submitted to HUD. As a result, the City did not accurately report the accomplishments of its Empowerment Zone Program to HUD.

Federal Requirements

Article IV, Section A, of the Grant Agreement for the City of Minneapolis' Empowerment Zone Program requires the City to submit annual reports to HUD on the progress made against its Empowerment Zone's Strategic Plan in accordance with 24 CFR Part 598.415. Annual reports must be in a format required by HUD.

24 CFR Part 598.415(a) requires Empowerment Zones to submit periodic reports to HUD identifying actions taken in accordance with their strategic plans, and providing notice of updates and modifications to their plans.

Page 2 of the Empowerment Zone and Enterprise Community Initiative Performance Measurement System guidance issued in April 2001 states that HUD is congressionally mandated to obtain performance reports from the Empowerment Zones. To accomplish this objective, the Zones are to report projects and progress via HUD's Performance Measurement System. The Empowerment Zones are required to submit an Annual Report that includes information on their progress for the projected outputs and milestones in the Zones' Implementation Plans. Page 14 of the Performance Measurement System guidance states milestones are the major steps taken to implement a project. Page 16 of the Performance Measurement System guidance states outputs

are the results immediately created upon implementation of a project or program.

Page 1 of the Renewal Communities/Empowerment Zones/Enterprise Communities Performance Measurement System User Guide issued in July 2002, which applies to the June 30, 2002 Annual Reports, states that HUD is congressionally mandated to obtain performance reports from the Empowerment Zones. To accomplish this objective, the Zones are to report projects and progress via HUD's Performance Measurement System. The Empowerment Zones are required to submit an Annual Report that includes information on their progress for the projected outputs and funding in the Zones' Implementation Plans. Page 12 requires the sources of funds should reflect the total projected monies over the life of the project. Page 24 states that outputs are the results immediately created upon implementation of a project or program.

The City Incorrectly Reported The Progress Of Empowerment Zone Projects

The City of Minneapolis inaccurately reported the accomplishments for seven of the 10 projects we reviewed from its June 30, 2001 or June 30, 2002 Annual Reports. The City's June 2001 Report contained inaccuracies related to three projects' progress on projected outputs and one project's percentage of completion on project milestones. The City's June 2002 Report contained inaccuracies related to two projects' progress on projected outputs and one project's source of funding. The following table shows the incorrect reporting by category for the seven projects and the page number in this report where a detailed summary for each project is located.

Project	Outputs	Milestones	Source of Funds	Page Number
Plymouth Christian Youth Center	X			28
Minneapolis Public School Wireless Technology	X			30
Agape 24-Hour Child Development Center	X			32
Green Institute	X			34
Near North Phase 1B			X	36
Park Plaza		X		38
Near North Planning and Development	X	-	-	40
Totals	<u>5</u>	<u>1</u>	<u>1</u>	

The City Inaccurately Reported Projects' Outputs

The City incorrectly reported five projects' outputs. Outputs are the results immediately created upon completion of a project. For example, the City reported in its June 30, 2002 Annual Report that the Plymouth Christian Youth Center project created or retained seven Empowerment Zone resident jobs and served 500 Zone residents. Documentation maintained by Plymouth Christian Youth Center showed that two Zone resident jobs were created or retained and only 88 Zone residents were served as of June 30, 2002.

The City Inaccurately Reported A Project's Milestones

The City inaccurately reported three milestones for one project. Milestones are the major steps taken to implement a project. The City reported in its June 30, 2001 Annual Report that three of Park Plaza project's five milestones were not applicable as of June 2001. Documentation maintained by Minneapolis Community Development Agency, the administering entity for the project, showed that the project completed the three milestones in December 2000. The three milestones were: secure additional construction assistance; finalize elevator work; and complete first building.

The City Inaccurately Reported A Project's Source Of Funding

The City inaccurately reported a source of funding for one project. Funds are the total projected monies over the life of a project. The City reported in its June 30, 2001 Annual Report that the Minneapolis Public Housing Authority provided \$400,000 for the Near North Phase 1B project as of June 2001. Documentation maintained by McCormack Baron and Associates, Inc., the administering entity for the

project, showed that the Authority only provided \$200,000 for the project as of June 30, 2001.

The City Lacked Effective Controls And Oversight Over Its Reporting

The City did not maintain adequate controls over its Annual Reports submitted to HUD. The Director of the City's Empowerment Zone said the City did not have the time to verify the accomplishments reported for each of its Zone projects. As a result, the City did not accurately report the accomplishments of its Empowerment Zone Program to HUD.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 46 and 53 to 57, contains the complete text of the comments for this finding.]

The City of Minneapolis' Empowerment Zone has met the Federal requirements with regards to reporting progress and outcomes of its Empowerment Zone funded projects. All Empowerment Zone contracts with the projects' administering entities require that annual reports be submitted by June 30th of each year and at the completion of the projects. A reporting template is created based on the projected milestones and outcomes submitted through HUD's Performance Measurement System. The template is also attached to all Zone contracts. A reminder letter is sent in May to all administering entities with the template and a reminder of the due date. Follow-up phone calls are made in June to all administering entities that have not submitted reports. HUD does not state in its reporting guidance or by contract that an Empowerment Zone is required to independently verify every outcome and result listed in an administering entity's reports.

The City concurs that some information submitted to HUD may have been inaccurately reported to the City. The information was not intended to be misleading, but was either mistakenly over reported or in some instances under reported.

The City of Minneapolis' Empowerment Zone concurs that based on documentation initially provided to the Office of Inspector General's auditors by Plymouth Christian Youth

Center, the number of Empowerment Zone residents served may have been over stated. The Center estimated that at least 500 of the over 2,000 neighborhood residents served resided in the Empowerment Zone. Some of the residents' addresses were not documented because addresses were not collected at all events. The Center will be recording addresses to document the benefits to Empowerment Zone residents. The 500 Empowerment Zone residents served could also be interpreted as an estimate based on the number of possible family members each of the 88 Zone children served by the Center could have.

The milestones for the Park Plaza project were not inaccurately reported. All milestones for the project were reported as not applicable in the City's June 30, 2001 Annual Report because the Memorandum of Agreement for the project was not executed until after June 2001. Furthermore, the draw down of funds for the project was not completed until after June 30, 2001. For these reasons, all of the milestones were recorded as not applicable.

Based on the previously mentioned information, the City requests that the Plymouth Christian Youth Center and Park Plaza projects be removed from Finding 1.

The City of Minneapolis' Empowerment Zone concurs that it incorrectly reported that the Minneapolis Public Housing Authority provided \$400,000 for the Near North Phase 1B project.

The City of Minneapolis' Empowerment Zone expects to hire a new project coordinator in January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its reporting controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.

OIG Evaluation Of Auditee Comments

The City did not follow HUD's Performance Measurement System guidance regarding its Annual Reports to HUD. Therefore, the City failed to accurately report the accomplishments of its Empowerment Zone Program to HUD. In order for HUD to assess the progress of the Empowerment Zone Program, the City should provide HUD

with accurate information regarding the progress of its Program.

The City did not provide supporting documentation for the number of Empowerment Zone resident jobs created and residents served by the Plymouth Christian Youth Center project. Documentation provided by the Center showed that two Zone resident jobs were created or retained and only 88 Zone residents were served as of June 30, 2002. Therefore, the City inaccurately reported the project's outputs.

The City reported in its June 30, 2001 Annual Report that three of Park Plaza project's five milestones were not applicable as of June 2001. Documentation maintained by Minneapolis Community Development Agency, the administering entity for the project, showed that the project completed the three milestones in December 2000. The three milestones included: secure additional construction assistance; finalize elevator work; and complete first building. Therefore, the City inaccurately reported three of the project's milestones to HUD.

The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.



Recommendations

We recommend that HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative assure the City of Minneapolis:

- 1A. Implements procedures and controls to verify the accuracy of information submitted to HUD for the City's Empowerment Zone Program.
- 1B. Ensures that staff responsible for preparing its Annual Report for HUD, use the actual verified accomplishments to report each project.

The City Provided Zone Funds To Projects That Have Not Benefited Zone Residents Or Benefited Between 3 And 38 Percent Of Zone Residents

The City of Minneapolis used all of its \$1,825,000 in Empowerment Zone monies committed to fund seven projects that have not benefited Empowerment Zone residents or benefited only 3 to 38 percent of Zone residents as of June 2002. Five of the seven projects are scheduled for completion between December 2003 and December 2011, and the remaining two projects were completed between December 2001 and July 2002. Since the five projects spent all of their Zone funds committed, benefits to Empowerment Zone residents would be expected. However, this has not occurred. The problem occurred because the City did not ensure that its Empowerment Zone contracts required projects to primarily benefit Zone residents. We believe the City's use of Empowerment Zone funds for the seven projects does not meet HUD's Empowerment Zone regulation at 24 CFR Part 598.215(b)(4)(i)(D) that incorporates the Appendix from the April 16, 1998 Federal Register requiring all projects financed in whole or in part with Zone funds be structured to primarily benefit Zone residents. However, HUD must make a determination whether the City's use of Zone funds was appropriate.

Federal Requirements

Page 1 of the Memorandum of Agreement dated June 29, 1999, between the City of Minneapolis and HUD, requires the City to comply with HUD's Empowerment Zone regulations at 24 CFR Part 598.

24 CFR Part 598.215(b)(4)(i)(D) states a detailed plan that outlines how an Empowerment Zone will implement its strategic plan must include details about proposed uses of Zone funds in accordance with guidelines published on April 16, 1998 in the Federal Register's Appendix.

Paragraph (3)(f) of the April 16, 1998 Federal Register, Appendix-Guidelines on Eligible Uses of Empowerment Zone Funds, requires all programs, services, and activities financed in whole or in part with Round II Empowerment Zone funds must be structured to primarily benefit Zone residents. The program, services, and activities may also benefit non-Zone residents.

Projects Have Not Benefited Zone Residents Or Benefited Less Than 50 Percent Of Zone Residents

The City used all of its \$1,825,000 in Empowerment Zone monies committed to fund seven projects that have not benefited Empowerment Zone residents or benefited only 3 to 38 percent of Zone residents as of June 2002. Five of the seven projects are scheduled for completion between December 2003 and December 2011, and the remaining two projects were completed between December 2001 and July 2002. Since the five projects spent all of their Zone funds committed, benefits to Empowerment Zone residents would be expected. However, this has not occurred. We believe the City's use of Empowerment Zone funds for the seven projects does not meet HUD's Empowerment Zone regulation at 24 CFR Part 598.215(b)(4)(i)(D) that incorporates the Appendix from the April 16, 1998 Federal Register requiring all projects financed in whole or in part with Zone funds be structured to primarily benefit Zone residents.

The following table shows for each of the seven projects as of June 2002: the actual start date; the estimated or actual completion date; Empowerment Zone funds committed; Zone funds spent; total number of individuals served; actual number of Zone residents served; and the percentage of Zone residents served.

Project	Actual Start Date	Projected/Actual Completion Date	Zone Funds Committed To Project	Zone Funds Spent On Project	Total Number Of Individuals Served	Number Of Zone Residents Served	Percentage Of Zone Residents Served
Opportunity Kitchen	7/1/01	8/1/06	\$250,000	\$250,000	0	0	0
Near North Phase 1B	1/5/01	12/31/01	\$200,000	\$200,000	0	0	0
Coliseum	11/29/00	11/30/10	\$300,000	\$300,000	65	2	3
Park Plaza	3/6/01	7/2/02	\$400,000	\$400,000	15	1	7
Plymouth Christian Youth Center	10/15/01	12/31/11	\$175,000	\$175,000	421	90	21
Agape 24-Hur Child Development Center	11/1/00	12/31/05	\$300,000	\$300,000	200	53	27
Hawthorne Homesteading	3/6/01	12/31/03	<u>\$200,000</u>	<u>\$200,000</u>	13	5	38
Totals			<u>\$1,825,000</u>	<u>\$1,825,000</u>			

The City executed contracts between November 29, 2000 and July 27, 2001 with the seven projects' administering entities. None of the City's contracts required the projects to primarily serve Empowerment Zone residents. Additionally,

the April 16, 1998 Federal Register does not provide a definition of primarily benefits Empowerment Zone residents. HUD issued a memorandum on July 2, 2002 that provided guidance to Empowerment Zones regarding benefits to Zone residents.

HUD's July 2002 memorandum states HUD presumes an Implementation Plan is consistent with an Empowerment Zone's strategic plan if at least a majority, 51 percent, of the beneficiaries of an activity are Zone residents. The memorandum also states that in computing the percentage of beneficiaries who are Zone residents where the benefit is in the form of jobs, at least 35 percent of those jobs must be filled by Zone residents. Since HUD's memorandum was issued after the seven projects were started, the memorandum cannot be used retroactively to determine the appropriateness of Empowerment Zone funds used for the projects. Therefore, HUD must make a determination whether the City's use of Zone funds for the seven projects was appropriate.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 47 to 49 and 58 to 61, contains the complete text of the comments for this finding.]

The Appendix from the April 16, 1998 Federal Register that the Office of Inspector General refers to states Empowerment Zones/Enterprise Communities Social Service Block Grant funding must be structured to primarily benefit Empowerment Zone residents and the programs may also benefit non residents. The City's Empowerment Zone has not invested or received any funding from the Department of Health and Human Services' Social Service Block Grant. Therefore, it is questionable as to whether the Appendix can be applied to funding received from HUD.

HUD has not provided a definition of primary benefit to Empowerment Zone residents that would apply to the projects reviewed. HUD's Office of Inspector General uses a July 2, 2002 memorandum from HUD's Assistant

Secretary for Community Planning and Development as their definition of primary benefit. HUD's memorandum is the only place where there is any reference to 50 percent or more of the benefits must go to Zone residents. HUD informed the Office of Inspector General several times that this memorandum cannot be applied retroactively. The definitions of individuals and residents served are a subjective interpretation by HUD's Office of Inspector General.

The goal of the Opportunity Kitchen project is to prepare 2,000 meals a week for needy families. It is the goal of the Minneapolis Empowerment Zone to use this project to provide training in food handling for difficult to employ Empowerment Zone residents. The Office of Inspector General reports that this project served no one, but it does report that the project has only been operating since October 2001. The project has only had two pilot training classes as of June 30, 2002. The Office of Inspector General also did not consider anyone who received a meal prepared to be a beneficiary of the project.

The beneficiaries of the Near North Phase 1B project can be construed to be all the residents who moved into the new public and affordable housing or no one as HUD's Office of Inspector General contends. That no individuals were served or benefited is not true. At the time of the project's contract closing and the loan payback, no one had moved into the project because it was not built. As of November 1, 2002, 10 families moved into the project. More than 100 families more will move in by February 1, 2003 and more than 700 families by the time the project's four phases are completed. The Empowerment Zone funding for the Near North Phase 1B project was paid back with interest.

Regarding the Coliseum project, HUD's Office of Inspector General did not include the number of individuals served or the number of Empowerment Zone residents served by all of the project's tenants. It is the City's contention that many more Zone residents benefited from the renovation of the project than the Office of Inspector General noted. The City is currently collecting information on all the individuals who received services from the project's tenants.

HUD's Office of Inspector General reports that only one Empowerment Zone resident was served by the Park Plaza project. We believe the Office of Inspector General only counted the number of Zone residents hired by the project's construction contractors who performed renovation work and did not take into consideration the number of Zone residents who reside in the project. Park Plaza is a 134-unit project based HUD Section 8 apartment complex located in the North Minneapolis Empowerment Zone. All five of the project's buildings are in the Empowerment Zone and were renovated with the assistance of Zone funds. In the City's opinion, all the families residing in the 134 units are Zone residents and benefited from the Empowerment Zone investment used to renovate the project's buildings. Therefore, it should be reported that 100 percent of the benefits of this project accrued to Zone residents.

The Office of Inspector General's total number of individuals served and Zone residents that benefited from the Plymouth Christian Youth Center project is based on the number of students attending the school. The number of individuals served and Zone resident does not include all of the organizations, area business people, and residents who benefited from the project. Attached is a list of the number of people who attended various community events at the Center. Thus, making the contention only 90 Empowerment Zone residents benefited from the project invalid.

Hawthorne Homesteading project's intent was to build new single-family homes on vacant lots in the City's Hawthorne neighborhood. HUD's Office of Inspector General reports that only two Empowerment Zone residents were served by the project. However, the project helped six families obtain new homes in the Empowerment Zone. Since every one of the homes built with Empowerment Zone funds is located in the Zone, the City contends that 100 percent of the project's benefits accrued to Zone residents. Documentation showing the list of addresses of the new homes in the Zone is attached.

The City cannot contend the 53 Empowerment Zone residents served by the Agape 24-Hour Child Development Center project.

Based on the previously cited information, the City requests that the Near North Phase 1B; Park Plaza; and Hawthorne Homesteading projects be removed from Finding 2.

The City of Minneapolis' Empowerment Zone agrees with the Recommendation to implement procedures and controls to ensure that Empowerment Zone contracts meet Empowerment Zone requirements regarding benefits to Zone residents. The City will continually strengthen its procedures to ensure Zone residents benefit from its project investments. This includes the new project coordinator position and project management software.

There is no HUD regulation defining primary benefits to Empowerment Zone residents. Therefore, the City does not agree with the Recommendation that HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative ensures the seven projects cited in this finding primarily benefit Empowerment Zone residents as required by the April 16, 1998 Federal Register. Additionally, the City disagrees that if HUD determines that the projects do not primarily benefit Zone residents, then HUD should require the City of Minneapolis to reimburse its Empowerment Zone Program the applicable amount from non-Federal funds.

OIG Evaluation Of
Auditee Comments

24 CFR Part 598.215(b)(4)(i)(D) states a detailed plan that outlines how an Empowerment Zone will implement its strategic plan must include details about proposed uses of Zone funds in accordance with guidelines published in the April 16, 1998 Federal Register's Appendix. Since the Appendix is made applicable by HUD's regulation, the requirements in the Appendix are applicable.

We agree that there is no regulatory or statutory definition regarding resident benefit. As stated in our audit report, the Appendix in the April 16, 1998 Federal Register does not provide a definition of primarily benefits to Empowerment Zone residents. Again, HUD must make a determination whether the City's use of Zone funds for the seven projects was appropriate.

As our audit report states, since HUD's July 2002 memorandum was issued after the City's seven projects were started, the memorandum cannot be used retroactively to determine the appropriateness of the Empowerment Zone funds used for the projects. Therefore, HUD must make a determination whether the City's use of Zone funds for the seven projects was appropriate.

The City did not provide sufficient documentation to support the number of residents served and the number of Zone residents served by the seven projects. Additionally, the City did not provide documentation to support its claim that the Empowerment Zone funding for the Near North Phase 1B project was repaid. Therefore, the project was not removed from our audit report.

We adjusted our audit report to include the five children served by the Hawthorne Homesteading project. This increased the number of individuals served and the number of Zone residents served to 13 and five, respectively. Therefore, 38 percent of the individuals served by the project were Zone residents.

The City needs to implement procedures and controls to ensure that Empowerment Zone contracts meet Empowerment Zone Program requirements regarding benefits to Zone residents.

HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative needs to ensure the seven projects cited in this finding primarily benefit Empowerment Zone residents as required by the April 16, 1998 Federal Register. If HUD determines that the projects do not primarily benefit Zone residents, then HUD should require the City to reimburse its Empowerment Zone Program the applicable amount from non-Federal funds.

Recommendations

We recommend that HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative assure the City of Minneapolis:

- 2A. Implements procedures and controls to ensure that Empowerment Zone contracts meet Empowerment

Zone Program requirements regarding benefits to Zone residents.

- 2B. Amend the contracts for the five projects cited in this finding scheduled for completion between December 2003 and December 2011 to include requirements regarding benefits to Zone residents.

We also recommend that HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative:

- 2C. Ensures the seven projects cited in this finding primarily benefit Empowerment Zone residents as required by the April 16, 1998 Federal Register. If HUD determines that the projects do not primarily benefit Zone residents, then HUD should require the City of Minneapolis to reimburse its Empowerment Zone Program the applicable amount from non-Federal funds.

Controls Over Empowerment Zone Funds Need To Be Improved

The City of Minneapolis needs to improve its oversight of Empowerment Zone funds. One of the 10 projects we reviewed inappropriately used \$9,705 of Zone funds to pay expenses not related to the City's Near North Planning and Development project. Since the City spent over \$3.6 million in Empowerment Zone funds as of May 2002 for the 10 projects, the City's inappropriate use of Zone funds was not a systematic break down in its controls over the Empowerment Zone Program. The problem occurred because the City did not adequately monitor the Near North Planning and Development project to ensure the use of Empowerment Zone funds was appropriate. As a result, the City needs to strengthen its controls over the use of Zone funds.

Federal Requirements

Article I, Section D, of the Grant Agreement for the City of Minneapolis' Empowerment Zone Program requires the City to comply with Office of Management and Budget Circular A-87, Cost Principles for State, Local, and Indian Tribal Governments.

Office of Management and Budget Circular A-87, Attachment A, paragraph C(3)(a) states that a cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.

The City Needs To Improve Its Controls Over Zone Funds

The City did not maintain adequate oversight for one of its 10 Empowerment Zone projects we reviewed. The City executed contracts with the Minneapolis Community Development Agency, the Minneapolis Public Housing Authority, and/or McCormack Baron and Associates to provide planning and development services for the Near North Planning and Development project, a mixed-use housing community. The City provided \$1,425,000 in Zone funds for the project.

The City inappropriately used \$9,705 in Empowerment Zone funds to reimburse The 106 Group, a consulting company, for expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process. The Zone funds used to reimburse The 106 Group were committed to the

Near North Planning and Development project. However, the expenses were not permitted according to the City's contract for the project.

The Director of the City's Empowerment Zone said since developing the guide and pamphlet was in the City's HUD-approved Implementation Plan for the Near North project, the City was allowed to use its Zone funds to pay The 106 Group. The Director also said that if the guide and pamphlet were developed today, administrative funds would be used to pay the expenses. However, the City was required to follow Office of Management and Budget Circular A-87 that states a cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received. Since the City's contract did not include any provision to pay the costs related to the guide and pamphlet, the City was prohibited from using Zone funds for the Near North Planning and Development project to pay the expense. As a result, the City needs to strengthen its controls over the use of Zone funds.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 49 to 50, contains the complete text of the comments for this finding.]

The City concurs that it inappropriately used \$9,705 of Empowerment Zone funds to pay expenses that were not related to the Near North Planning and Development project. HUD approved the expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process as a line item through the Performance Measurement System. At no time did anyone at HUD indicate that this was not an appropriate area to charge the expenses.

The Section 106 review is required as a result of Federal funding for a project. The Near North project was going through that 106 process utilizing The 106 Group for guidance. As a result of the City's involvement in this process, it was determined that it would be in the best interest of all future Empowerment Zone funded projects

that the City develop materials to inform applicants about the process. By adding an additional \$12,000 to the Near North 106 consulting contract, the City was able to achieve the goal for a fraction of the time and cost of going through the process independent of the Near North project. This agreement is an example of efficient government and reduced bureaucracy. It saved thousands of dollars and hundreds of staff time hours over the last three years and even came in 20 percent under the projected budget.

The City does not agree that it should reimburse its Empowerment Zone Program from non-Federal funds. The expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process is an eligible use of Empowerment Zone funds. The expenditure should be charged to the Zone's general administration. The City suggests that it credit the Near North Planning and Development project \$9,705 and debit its Empowerment Zone Administration \$9,705.

OIG Evaluation Of Auditee Comments

We adjusted our audit report to show that since the City's contract did not include any provision to pay the expenses related to the guide and pamphlet, the City was prohibited from using Zone funds for the Near North Planning and Development project to pay the expenses. We also adjusted our Recommendation to state that the City should reimburse its Near North Planning and Development project \$9,705 from Empowerment Zone Administration funds for the improper use of Zone funds cited in this finding. The City needs to improve its procedures and controls to ensure that Empowerment Zone funds are used efficiently and effectively, and in accordance with Empowerment Zone Program requirements.

Recommendations

We recommend that HUD's Director of Renewal Communities/Empowerment Zones/Enterprise Communities Initiative assure the City of Minneapolis:

- 3A. Reimburses its Near North Planning and Development project \$9,705 from Empowerment

Zone Administration funds for the improper use of Zone funds cited in this finding.

- 3B. Improves its procedures and controls to ensure that Empowerment Zone funds are used efficiently and effectively, and in accordance with Empowerment Zone Program requirements.

Management Controls

Management controls include the plan of organization, methods, and procedures adopted by management to ensure that its goals are met. Management controls include the processes for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Management Controls

We determined that the following management controls were relevant to our audit objectives:

- Program Operations - Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Validity and Reliability of Data - Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with Laws and Regulations - Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding Resources - Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed all of the relevant controls identified above during our audit of the City of Minneapolis' Empowerment Zone Program.

It is a significant weakness if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet an organization's objectives.

Significant Weaknesses

Based on our review, we believe the following items are significant weaknesses:

- Validity and Reliability of Data

The City incorrectly reported the actual status and/or progress for seven of the 10 projects we reviewed from its June 30, 2001 or June 30, 2002 Annual Reports. The City's June 2001 Report contained inaccuracies related to three projects' progress on projected outputs and one project's percentage of completion on project milestones. The City's June 2002 Report contained inaccuracies related to two projects' progress on projected outputs and one project's source of funding (see Finding 1).

- Compliance with Laws and Regulations

The City failed to follow HUD's regulation regarding the reporting of actual status and/or progress for seven of the 10 projects we reviewed from its June 30, 2001 or June 30, 2002 Annual Reports (see Finding 1).

Follow Up On Prior Audits

This is the first audit of the City of Minneapolis, Minnesota's Empowerment Zone Program by HUD's Office of Inspector General. The latest Independent Auditors' Report for the City covered the period ending December 31, 2001. The Report contained no findings.



Schedule Of Ineligible Costs

<u>Recommendation</u>	
<u>Number</u>	<u>Ineligible Costs 1/</u>
3A	<u>\$9,705</u>
Total	<u>\$9,705</u>

1/ Ineligible costs are costs charged to a HUD-financed or insured program or activity that the auditor believes are not allowable by law, contract, or Federal, State, or local policies or regulations.



Projects Reviewed

This appendix contains the individual evaluations for the projects we reviewed. We selected 10 of the City of Minneapolis' 20 projects reported in its June 30, 2001 or June 30, 2002 Annual Reports. We found that the City inaccurately reported the accomplishments of its Empowerment Zone Program to HUD for seven projects and inappropriately used Empowerment Zone funds for one project. The following table shows the seven projects that had problems, the location of their evaluation in this appendix, and the finding(s) they relate to.

<i>Project</i>	<i>Page</i>	<i>Finding</i>
Plymouth Christian Youth Center	28	1
Minneapolis Public School Wireless Technology	30	1
Agape 24-Hour Child Development Center	32	1
Green Institute	34	1
Near North Phase 1B	36	1
Park Plaza	38	1
Near North Planning and Development	40	1 and 3

Accomplishments Of Plymouth Christian Youth Center Project Was Inaccurately Reported

The City of Minneapolis incorrectly reported two outputs for its Plymouth Christian Youth Center project in the City's June 30, 2002 Annual Report. The City inaccurately reported the number of Empowerment Zone resident jobs created or retained and the number of Zone residents served. The inaccurate reporting occurred because the City did not verify the accuracy of the information the project's administering entity provided for the City's June 2002 Annual Report. As a result, the City did not provide HUD with an accurate representation of the project and the impression exists that the benefits of the project are greater than actually achieved.

The City Inaccurately Reported Project's Outputs

The City reported in its June 30, 2002 Annual Report that the Plymouth Christian Youth Center project created or retained seven Empowerment Zone resident jobs and served 500 Zone residents. Documentation maintained by the Center showed that only two resident jobs were created or retained and only 88 Zone residents were served.

The Planner II for the City's Empowerment Zone said the City did not verify the accomplishments the Center reported for the project. The Director for the City's Empowerment Zone said the City did not have time to verify the accomplishments reported for each of its administering entities. As a result, the City did not accurately report the accomplishments of its Empowerment Zone Program to HUD. The impression exists that the benefits of the project were greater than actually achieved.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 53 to 54, contains the complete text of the comments for this project.]

The City concurs that based on the documentation initially provided to the Office of Inspector General's auditors by Plymouth Christian Youth Center, the number of Empowerment Zone residents served may have been overstated. The Center estimated that at least 500 of the over 2,000 neighborhood residents served resided in the

Empowerment Zone. Some of the residents' addresses were not documented because they were not collected at all events. The Center will be recording addresses to document the benefit to Empowerment Zone residents.

The 500 Empowerment Zone residents served could also be interpreted as an estimate based on the number of possible family members each of the 88 Zone children served by the Center could have.

Based on the previously cited information, the City requests this finding on the Plymouth Christian Youth Center project be removed from the report.

The City expects to hire a new project coordinator by the end of January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.



OIG Evaluation Of
Auditee Comments

The City did not provide supporting documentation for the number of Empowerment Zone resident jobs created or the Zone residents served by the Plymouth Christian Youth Center project to warrant removal of this project from our audit report.

The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.

An Output Of Minneapolis Public School Wireless Technology Project Was Inaccurately Reported

The City of Minneapolis inaccurately reported an output for its Minneapolis Public School Wireless Technology project. The City inaccurately reported in its June 30, 2001 Annual Report the number of Empowerment Zone children served by the project. The inaccurate reporting occurred because the City did not verify the accuracy of the information its administering entities provided for the City's Annual Report. As a result, the City did not provide HUD with an accurate representation of the project and the impression exists that the benefits of the project are greater than actually achieved.

The City Inaccurately Reported Project's Output

The City reported in its June 30, 2001 Annual Report that the Minneapolis Public School Wireless Technology project served 1,728 Empowerment Zone children. Documentation maintained by the Minneapolis Public School, the administering entity of the Minneapolis Public School Wireless Technology project, showed that only 981 Empowerment Zone children were served.

The Planner II for the City's Empowerment Zone said the City did not verify the accomplishments reported for the project by the Minneapolis Public School. As a result, the impression exists that the benefits of the project were greater than actually achieved.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 54 to 55, contains the complete text of the comments for this project.]

The City concurs that it incorrectly reported the number of Empowerment Zone children served by the Minneapolis Public School Wireless Technology project and that it did not verify the accomplishments reported for the project by the Minneapolis Public School, the administering entity of the project.

The City expects to hire a new project coordinator by the end of January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.



OIG Evaluation Of
Auditee Comments

The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.

Accomplishments Of Agape 24-Hour Child Development Center Project Were Inaccurately Reported

The City of Minneapolis did not accurately report two outputs for its Agape 24-Hour Child Development Center project. The City inaccurately reported in its June 30, 2001 Annual Report the number of homeless and other human service programs operated through the Agape 24-Hour Child Development Center. The inaccurate reporting occurred because the City did not verify the accuracy of the information its administering entities provided for the City's Annual Report. As a result, the City did not provide HUD with an accurate representation of the project and the impression exists that the benefits of the project are greater than actually achieved.

The City Inaccurately Reported Project's Outputs

The City reported in its June 30, 2001 Annual Report that the Agape 24-Hour Child Development Center project operated eight homeless programs and 12 other human service programs. Documentation maintained by Oasis of Love, Inc., the administering entity for the project, showed that no homeless programs or other human service programs were operated in connection with the project.

The Planner II for the City's Empowerment Zone said the City did not verify the accomplishments Oasis of Love, Inc. reported for the project. As a result, the impression exists that the benefits of the project were greater than actually achieved.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, page 55, contains the complete text of the comments for this project.]

The Agape 24-Hour Child Development Center project provides 24-hour childcare services. The project works mainly with domestically abused women who are homeless as a result of being forced to leave an abusive environment. Oasis of Love, Inc, the administering entity for the project, and the project work with the women and their families, and refer them to organizations that can provide housing and

other services. Although Oasis of Love might not operate the programs reported, Oasis of Love is a well-known source of referrals and has numerous partnering agencies.

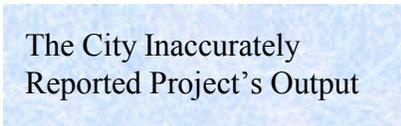


OIG Evaluation Of
Auditee Comments

The City reported in its June 30, 2001 Annual Report that the Agape 24-Hour Child Development Center project operated eight homeless programs and 12 other human service programs. Documentation maintained by Oasis of Love, Inc., the administering entity for the project, showed that no homeless programs or other human service programs were operated in connection with the project. While Oasis of Love might be a well-known source referrals and may have numerous partnering agencies, the City must ensure the accuracy of the Annual Reports so HUD can have an accurate representation of the City's Empowerment Zone Program.

An Output Of Green Institute Project Was Inaccurately Reported

The City of Minneapolis did not accurately report an output for its Green Institute project in the City's June 30, 2002 Annual Report. The City inaccurately reported the number of Empowerment Zone resident jobs created or retained by the project. The inaccurate reporting occurred because the City did not verify the accuracy of the information its administering entities provided for the City's Annual Report. As a result, the City did not provide HUD with an accurate representation of the project.

The City Inaccurately Reported Project's Output

The City inaccurately reported in its June 30, 2002 Annual Report the number of Empowerment Zone resident jobs created or retained as a result of the Green Institute project. The City reported that five Empowerment Zone resident jobs were either created or retained at the Green Institute or its tenant, the Minneapolis Transit Constructors. Documentation maintained by the Green Institute showed that nine Zone resident jobs were created or retained at the Green Institute or the Minneapolis Transit Constructors.

The Planner II for the City's Empowerment Zone said the City did not verify the accomplishments the Green Institute reported for the project. As a result, the City did not provide HUD with an accurate representation of the project.



Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 55 to 56, contains the complete text of the comments for this project.]

The City reported that 20 Empowerment Zone resident jobs were projected to be created or to be retained, and five Zone resident jobs were created or retained as of June 30, 2002. Although the City inaccurately under reported the number of Zone resident jobs created or retained by four, it did not over report the number of Zone resident jobs created or retained. This finding on the Green Institute project should be removed from the report because Zone funds were not used

and the Green Institute did not over report the number of Zone resident jobs created or retained.

The City expects to hire a new project coordinator by the end of January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.



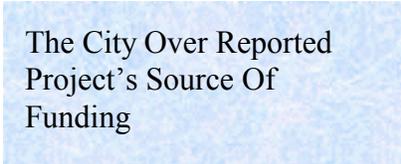
OIG Evaluation Of Auditee Comments

We adjusted our audit report to show that the City reported that five Empowerment Zone resident jobs were either created or retained at the Green Institute or its tenant, the Minneapolis Transit Constructors. Documentation maintained by the Green Institute showed that nine Zone resident jobs were created or retained at the Green Institute or the Minneapolis Transit Constructors. As a result, the City did not provide HUD with an accurate representation of the project.

While the City under reported the Green Institute project's output, we did not remove this project from our report since the City inaccurately reported the project in its June 2002 Annual Report to HUD. The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.

Funding For The Near North Phase 1B Project Was Inaccurately Reported

The City of Minneapolis did not accurately report in its June 30, 2002 Annual Report the amount of funding for the Near North Phase 1B project. The inaccurate reporting occurred because the City lacked effective controls and oversight to ensure the accuracy of the source of funding reported in its Annual Report. As a result, the City did not provide HUD with an accurate representation of the project.

The City Over Reported Project's Source Of Funding

The City inaccurately reported in its June 30, 2002 Annual Report the amount of funding for the Near North Phase 1B project. The City reported that the Minneapolis Public Housing Authority provided \$400,000 for the project. Documentation maintained by McCormack Baron and Associates, Inc., the administering entity for the project, showed the Authority only provided \$200,000 for the project as of June 30, 2002.

The Program Coordinator for the City's Empowerment Zone said the City made a mistake in reporting that the Authority provided \$400,000 for the project. The Coordinator said the City included \$200,000 the Authority provided for another project. As a result, the impression exists that the project's funding is greater than actually achieved.



Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, page 56, contains the complete text of the comments for this project.]

The City concurs that it incorrectly reported that the Minneapolis Public Housing Authority provided \$400,000 for the project.

The City expects to hire a new project coordinator by the end of January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its

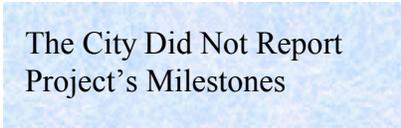
controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.

**OIG Evaluation Of
Auditee Comments**

The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.

Milestones Of Park Plaza Project Were Inaccurately Reported

The City of Minneapolis incorrectly reported three milestones for its Park Plaza project in the City's June 30, 2001 Annual Report. The City inaccurately reported that the milestones for the project were not applicable as of June 2001. The inaccurate reporting occurred because the City lacked effective controls and oversight to assure the accuracy of the project's milestones reported in the City's Annual Report. As a result, the impression exists that the accomplishments of the project are less than actually achieved.

The City Did Not Report Project's Milestones

The City reported in its June 30, 2001 Annual Report that three of Park Plaza project's five milestones were not applicable as of June 2001. Documentation maintained by Minneapolis Community Development Agency, the administering entity for the project, showed that the project completed the three milestones in December 2000. The three milestones included: secure additional construction assistance; finalize elevator work; and complete first building.

The Minneapolis Community Development Agency's Project Manager said she could not keep track of all the reports due for its various projects and relied on the City's Empowerment Zone staff to notify her when a report was due. However, she said the City did not notify her that a report should be completed; therefore, she did not submit a report.

The City's Planner II said the City did not receive a report for the Park Plaza project. The Planner II said she was not sure why the City did not receive a report or why the accomplishments of the project were not included in the City's June 30, 2001 Annual Report. As a result, the City did not provide HUD an accurate impression of the project's accomplishments.



Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on

our draft report follows. Appendix C, pages 56 to 57, contains the complete text of the comments for this project.]

The milestones for the Park Plaza project were accurately reported. All milestones for the project were reported as not applicable in the June 30, 2001 Annual Report because the Memorandum of Understanding for the project was not executed into until after June 2001. Furthermore, the draw down of funds for the project was not completed until after June 30, 2001. For these reasons, all of the milestones were recorded as not applicable. Based on this information, the City requests this finding on the Park Plaza project be removed from the report.

The City expects to hire a new project coordinator by the end of January 2003 and will also obtain project management software to ensure its timely reports to HUD.



OIG Evaluation Of Auditee Comments

The City reported in its June 30, 2001 Annual Report that three of Park Plaza project's five milestones were not applicable as of June 2001. Documentation maintained by Minneapolis Community Development Agency, the administering entity for the project, showed that the project completed the three milestones in December 2000. The three milestones included: secure additional construction assistance; finalize elevator work; and complete first building. While the City had not executed a Memorandum of Understanding until March 2001 or drawn down funds for the project, the project completed the three milestones by June 2001. Therefore, the City should have reported the three milestones to HUD as completed in December 2000.

Controls Over Near North Planning And Development Project Were Not Adequate

The City of Minneapolis did not maintain adequate controls over its Near North Planning and Development project. The City inappropriately used \$9,705 of the Empowerment Zone funds to pay expenses that were not related to the project. The City also did not accurately report in its June 30, 2001 Annual Report the project's output regarding resident participation in community meetings. The inappropriate use of the Zone funds and inaccurate reporting occurred because the City did not ensure the use of Empowerment Zone funds met the City's contract for the project and verify the accuracy of the information provided by the project's administering entity for the City's Annual Report. As a result, Empowerment Zone funds were not used efficiently and effectively. The City also did not provide HUD with an accurate representation of the project and the impression exists that the benefits of the project are less than actually achieved.



The City Lacked Adequate Controls Over Zone Funds

The City executed contracts with the Minneapolis Community Development Agency, the Minneapolis Public Housing Authority, and/or McCormack Baron and Associates, Inc. to provide planning and development services for the Near North Planning and Development project, a mixed-use housing community. The City provided \$1,425,000 in Zone funds for the project.

The City used \$9,705 in Empowerment Zone funds to reimburse The 106 Group, a consulting company, for expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process. The Zone funds used to reimburse The 106 Group were committed to the Near North Planning and Development project. However, the expenses were not permitted according to the City's contract for the project.

The Director for the City's Empowerment Zone said since developing the guide and pamphlet was in the City's HUD-approved Implementation Plan for the Near North project, the City was allowed to use its Zone funds to pay The 106 Group. The Director also said that if the guide and pamphlet were developed today, administrative funds would be used to cover the costs. However, the City was required to follow Office of Management and Budget Circular A-87 that states a cost is allocable to a particular cost objective if the goods

or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received. Since the City's contract did not include any provision to pay the costs related to the guide and pamphlet, the City was prohibited from using Zone funds for the Near North Planning and Development project to pay the expense.

The City Inaccurately Reported Project's Output

The City inaccurately reported in its June 30, 2001 Annual Report the number of residents participating in community meetings for the Near North Planning and Development project. The City reported 100 residents participated in community meetings. Documentation maintained by McCormack Baron and Associates, Inc., the administering entity for the project, showed that 354 residents participated in community meetings for the project.

The Planner II for the City's Empowerment Zone said the City did not verify the accomplishments that McCormack Baron and Associates, Inc. reported to the City for the Near North project. The Director for the City's Empowerment Zone said the City did not have time to verify the accomplishments reported by each of the projects' administering entities. As a result, the City did not provide HUD with an accurate representation of the project and the impression exists that the benefits of the project were less than actually achieved.

Auditee Comments

[Excerpts paraphrased from the comments provided by the Director of the City of Minneapolis' Empowerment Zone on our draft report follows. Appendix C, pages 49 to 50 and 57, contains the complete text of the comments for this project.]

The City concurs that it inappropriately used \$9,705 of Empowerment Zone funds to pay expenses that were not related to the Near North Planning and Development project. HUD approved the expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process as a line item through the Performance Measurement System. At no time did anyone at HUD indicate that this was not an appropriate area to charge the expenses.

The Section 106 review is required as a result of Federal funding for a project. The Near North project was going through that 106 process utilizing The 106 Group for guidance. As a result of the City's involvement in this process, it was determined that it would be in the best interest of all future Empowerment Zone funded projects that the City develop materials to inform applicants about the process. By adding an additional \$12,000 to the Near North 106 consulting contract, the City was able to achieve the goal for a fraction of the time and cost of going through the process independent of the Near North project. This agreement is an example of efficient government and reduced bureaucracy. It saved thousands of dollars and hundreds of staff time hours over the last three years and even came in 20 percent under the projected budget.

The City does not agree that it should reimburse its Empowerment Zone Program from non-Federal funds. The expenses associated with developing a guide and pamphlet for organizations required to go through the Section 106 Historic Preservation process is an eligible use of Empowerment Zone funds. The expenditure should be charged to the Zone's general administration. The City suggests that it credit the Near North Planning and Development project \$9,705 and debit its Empowerment Zone Administration \$9,705.

The City concurs that it incorrectly reported the number of residents participating in community meetings for the Near North Planning and Development project and that it did not verify the accomplishments reported for the project. The City did not think it was worth its time and money to verify the addresses of more than 500 people who attended the numerous community and task force meetings.

The City expects to hire a new project coordinator by the end of January 2003 to ensure more accurate reporting. The City will also obtain project management software to increase its controls and assist staff in ensuring the accuracy and oversight of the City's Annual Report to HUD.

related to the guide and pamphlet, the City was prohibited from using Zone funds for the Near North Planning and Development project to pay the expenses. We also adjusted our Recommendation to state that the City should reimburse its Near North Planning and Development project \$9,705 from Empowerment Zone Administration funds for the improper use of Zone funds cited in this finding. The City needs to improve its procedures and controls to ensure that Empowerment Zone funds are used efficiently and effectively, and in accordance with Empowerment Zone Program requirements.

The actions planned by the City to ensure accurate reporting should improve its reporting procedures, if fully implemented.



Auditee Comments



Minneapolis
City of Lakes

**Office of the Minneapolis
Empowerment Zone**

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Director

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December 26, 2002

Mr. Edward Kim, Assistant Regional Inspector General for Audit
U.S. Department of HUD - Office of Inspector General
200 North High Street, Room 334
Columbus, Ohio 43215

RE: Draft Response to the Draft Audit Findings dated December 11, 2002

Mr. Kim:

This letter is submitted in response to the draft Office of Inspector General (IG) audit of the Minneapolis Empowerment Zone (EZ). This response is in the format of the draft audit: introduction, findings and appendices.

Though the draft audit implies a negative tone in regards to the Minneapolis EZ program it does recognize, through omission, the successful implementation of this program. To summarize, all the projects reviewed are successfully implemented and/or completed. All audited EZ funds were accounted for and the projects had significant positive affects on the residents and business people of the EZ.

In the Introduction we question why the IG office used as the basis of a finding a congressional record appendix that refers to non-HUD funds, and a memo defining "primary benefit" that was written in July 2002 subsequent to the audit period ending April 30, 2002. The only federal funds received by the Minneapolis EZ, a Round II EZ, have been from HUD. Also, it is our knowledge that HUD informed the IG office that the July 2nd memo's definitions could not be applied retroactively.

The Draft Audit

INTRODUCTION:

Paragraph two of the introduction states that "the program was designed to provide \$250 million in tax benefits and \$100 million of Social Service Block Grant (SSBG) funds from the department of Health and Human Services (HHS)." This is not what has occurred in reality. This point becomes the basis for later responses calling into question the use of the appendix as the foundation of a finding. While the intent was to provide HHS SSBG funding to the program the Minneapolis EZ has not received or committed any SSBG funding to the projects reviewed. We recommend that any references to funds that the EZ has not received be deleted or clearly stated as "background information only". Including this information in the introduction of the audit is confusing and could easily be misleading. We also recommend that identification of the true source of Round II EZ funding, HUD, be added to the audit text. In addition, HUD's appropriation to Minneapolis' Empowerment Zone program through Fiscal Year 2002 totaled \$21.9 million. This is significantly different than the \$100 million implied in the draft introduction.

In the third paragraph it is also important to note that the Empowerment Zone program is managed by the Minneapolis City Council and Mayor, and a 30-member Governance Board that includes Empowerment Zone resident and business representatives.

FINDING 1:

The first three paragraphs under "Federal Requirements" list the requirements of the local EZ in regards to reporting progress and outcomes of EZ funded projects. The Minneapolis EZ has met all these requirements. All Minneapolis EZ sub-recipient contracts require that annual reports be submitted by June 30th of each year and at completion of the project. A reporting template is created based on the projected milestones and outcomes submitted to HUD through the Performance Measurement System (PERMS) and attached to all executed contracts. A reminder letter is sent in May to all sub-recipients with the template and a reminder of the due date. Follow up phone calls are made in mid-June to all sub-recipients who have not yet submitted reports. HUD does not state in procedure manuals or by contract that an EZ is required to independently verify every outcome and result listed in the sub-recipient reports.

In regards to this finding, we agree that some of the information submitted to HUD may have been reported inaccurately to our office. This information was not intended to be misleading, but was either mistakenly over reported or in some instances under reported. The lack of a agreed to definition of benefit must be considered in this case. Up to this point the sub-recipients and the Minneapolis EZ office are working off of assumptions about what is benefit. For each project or program it is different.

Therefore, based on further documentation and explanation provided in appendix B to this response, the City of Minneapolis is requesting that the following projects be removed from the findings: Plymouth Christian Youth Center, Green Institute and Park Plaza.

However, as a remedy to this finding's general issue and to ensure more accurate reporting, a new project coordinator position has been created at the Minneapolis EZ. The position is expected to be filled by the end of January 2003. This person will be given the charge to address and implement recommendations 1A and 1B. In addition, they will work on defining EZ benefit and standardizing the reporting of benefit.

The City will also invest in project management software tailored specifically to fit the HUD required Performance Measurement System (PERMS). This will increase controls and assist staff in ensuring accuracy and oversight in the annual report. This new system will begin immediately. It is modeled after the systems created for the Chicago Round I EZ and the Boston Round II EZ.

The specifics of each of the projects referred to in this section will be addressed as part of appendix B.

FINDING 2:

Paragraph one of this section refers to an Appendix to HUD's Empowerment Zone regulation at 24 CFR Part 598.215(b)(4)(i)(D) that incorporates the appendix from April 16, 1998. I have attached the referred to appendix to this letter. In this appendix IG auditors refer to the section that states "EZ/EC SSBG funding must be structured to primarily benefit EZ residents; the programs may also benefit non residents."

The Minneapolis EZ has not invested or received any HHS SSBG funding. Thus it is confusing at the least and entirely questionable whether this can be applied at all to funding received through HUD.

Second, HUD has provided no definition of "primary benefit" applicable to the projects reviewed. HUD IG uses a July 2, 2002 memo from HUD Assistant Secretary Bernardi as their definition of primary benefit. This memo is the only place where there is any reference to "50% or more" of the benefit must go to Zone residents. The IG office has been informed several times by the HUD EZ office, this memorandum can not be applied as a basis for a finding or used to define primary benefit, as it is not retroactive.

Third, while addressing each of the audit report's numbers of individuals served, residents served and percentage of zone residents served, is saved for the appendix, it should be observed that the definitions of "individuals and residents served" is a subjective interpretation by the IG auditors. For example, the auditors state that only one Empowerment Zone resident is served at Park Plaza. We believe they only counted the number of EZ residents who were hired by the construction contractors to renovate the buildings and they do not take into consideration the number of EZ residents who reside in the buildings. Park Plaza is a 134 unit project based HUD section 8 apartment complex located in the North Minneapolis EZ. All of the five buildings are in the EZ and were renovated with the assistance of EZ funds. In our opinion all the families residing in the 134 units of housing are EZ residents and have benefited from the EZ investment used to renovate the buildings. Therefore, it should be reported that 100% of the benefit of this project accrued to EZ residents.

Furthermore, until the final meeting with the auditors in November, the auditors mistakenly assumed that Park Plaza was not in the EZ. A review of evidence from the original 1998 Minneapolis EZ application convinced IG staff of its correct location in the EZ.

We are requesting that Park Plaza be removed from this finding. Documentation showing that 100% of the Park Plaza benefit went to Empowerment Zone residents, is attached and noted in Appendix B and C of this response. We are also asking that the Near North Phase IB and the Hawthorne Homesteading projects be removed from the list under this finding as well. Information and documentation related to this request is attached and noted in Appendix C.

On pages 7 and 8 of the draft audit referring to finding 2 it is stated that only 3 to 27 percent of Zone residents benefited as of June 2002. This is inaccurate and using a percentage is misleading. Information about other projects, such as documentation showing that 100% of the Park Plaza benefit went to Empowerment Zone residents, is attached and noted in the response to Appendix B.

Because the specifics of the projects listed in the chart on page 8 under finding two are not detailed in appendix A or B, I will respond to each of them in Appendix C of the Minneapolis EZ response to the December 12, 2002 audit findings.

Continuing through the report, in reference to the second paragraph on page 9 referring to the July 2, 2002 memo. This paragraph should be deleted from the report. Any audit reliance or general assumptions based on the July 2, 2002 memo are inappropriate to the reviewed projects for the subject audit period and should be removed before final publication of the report. The audit period ended April 30, 2002 and the July 2, 2002 memo is not retroactive.

Regarding the recommendations under Finding Two: The Minneapolis EZ agrees with recommendation 2A and we continually strengthen our procedures to ensure EZ residents benefit from our project investments. This will include the new full-time staff position and project management software program noted earlier.

As the auditors are aware, we also would like to arrive at resolving the definition of what zone resident benefit is. However, implying that the April 16, 1998 appendix defines how much benefit must be done is inappropriate for reasons stated above.

Finally, in regards to finding recommendation 2B. In the future, if HUD determines the definition of how much zone resident benefit must be adhered to in each project we will comply going forward. However, recommending HUD go back and apply a future primary benefit definition to these projects and requiring the City of Minneapolis to pay back funds if they do not comply with that definition is problematic for several reasons:

1. Prior to the City of Minneapolis expending funds, HUD through PERMS approved all of the expenditures as an eligible use of EZ funds.
2. All the EZ money invested in these projects was and is accounted for and spent according to approved plans.
3. Applying subjective definitions retroactively can not legally be done. For example, HUD senior legal counsel has stated that the July 2, 2002 memo is not enforceable, let alone retroactive, because Congress has not reviewed it or published in the federal register.
4. It is not entirely agreed to that the 1998 appendix referred to is enforceable in regards to HUD funds. Thus the basis of this finding must be called into question.

For all the reasons stated above we recommend that finding number 2, may better be stated as: "The City Provided Zone Funds to Projects That Have Not **Yet** Benefited **All intended Empowerment Zone and non-Empowerment Zone** Residents."

This would take into consideration the fact that the projects are still in progress and they will not have results that can not be documented until the project is further along. This would also correct the inaccurate assessment of documentation made during the audit.

In summary, regarding the recommendations under Finding Two: The Minneapolis EZ agrees with recommendation 2A and we continually strengthen our procedures to ensure EZ residents

benefit from our project investments. As stated under finding one this will include a new full-time staff position and project management software program noted earlier. The Minneapolis EZ does not agree with finding 2B. As stated earlier, when a definition of resident benefit is determined we will adhere to it and implement it as part of our project's performance. However, that definition is still not determined and thus the recommended action as listed in 2B is inappropriate and we request that it be removed from the audit.

FINDING 3:

We are glad to see that the IG auditors have confirmed that 99.74% of EZ dollars were spent appropriately. To state that "controls over EZ funds need to be improved" as a result of a potential finding that \$9,705 should have been charged against administration rather than the \$1.425 million master plan budget out of a total amount audited of \$3,697,000 is focusing only on the negative.

In regards to the second paragraph on page 12, what was being stated in this paragraph was not that the \$9,705 spent on the 106 programmatic agreement was inappropriate at the time, but rather that today and after participation in the audit, we can appreciate the IG auditors position that this expense may be more appropriately charged to overall administration of the Empowerment Zone programs as compared to the Near North Project.

It is important to note, however, that HUD approved this expenditure as a line item through the PERMS system and at no time did anyone at HUD indicate that this was not an appropriate area to charge this expense to.

It is also important to note that the Section 106 review is required to be done as a result of federal funding being invested into a project. The Near North project was going through that 106 process utilizing the 106 consulting group for guidance. As a result of the EZ's involvement in this process it was determined that it would be in the best interest of all future EZ funded projects that we develop materials to inform applicants about this process. By adding an additional \$12,000 to the Near North 106 consulting contract we were able to achieve the goal for a fraction of the time and cost of going through the process independent of the Near North project. The report should note that this agreement is an example of efficient government and reduced bureaucracy. It has saved thousands of dollars and hundreds of staff time hours over the last three years and even came in 20% under the projected budget.

In response to the recommendations: the City of Minneapolis does not agree that this amount should be paid out of non-federal funds. To state that this is an ineligible use of funds is not true. The use of EZ funding for a section 106 related expense is an eligible use of EZ funds. The only difference of opinion we have is what cost category it should be charged to - project specific of general administration?

Based on this point we suggest that the IG amend their audit report recommendation 3A to state that the Near North Project cost category be credited \$9,705 and EZ administration cost category be debited \$9,705.

In reference to recommendation 3B, we continue to work hard to enhance funding controls and the additional staff person will assure effective evaluation of all EZ funded project reports.

MANAGEMENT CONTROLS:

Considering again that all the funding was accounted for and that no written document expressly states that the EZ office is "required" to verify all the data submitted by sub-recipients and according to this report's findings 99.74% of the \$3,697,000 in audited EZ funding was appropriately spent we think we have good management controls in place. Moreover, as listed on page 15, in the latest independent audit done on the Minneapolis EZ for the period ending December 31, 2001 there were no findings. Claiming significant weakness of management is an overstatement.

However, regardless of audit stance, the City of Minneapolis will commit more resources and effort into the oversight of the projects and programs that receive EZ funding.

In conclusion, it is important to note that we disagree with much of this report. The report uses obscure appendices that at no time were presented by or made aware to us through any training program or direct communication from HUD. Within the 24 part 598 appendix there is no reference to HUD funding creating confusion as to its applicability to Round II HUD funded EZs. Furthermore, the referred to definition of "primary benefit" is not defined in the 24 Part 598 appendix or any congressional record. Rather, incorrectly the IG uses a memo written 60 days after the audit period and applied retroactively to review the Minneapolis projects. While we acknowledge that the audit states the definition is not used as the basis for the definition of "primarily benefit" its inclusion within the text lends a level of credibility to the IG's subjective definition used to establish findings in the report. The HUD EZ office has informed the IG that this definition can not be used in this audit. Again, we request that all references to it be taken out of the final report.

We would also like to make clear that the successful implementation of the Minneapolis EZ program is performed by 2 1/2 FTEs. Our administration costs to date amount to only 5% of the amount of EZ funding committed to projects. It is fair to assume that these administrative costs are effectively lean in comparison to other HUD programs.

It should be clear that we have a case for several of the projects to be removed from the findings. We are hopeful that the IG will respond to this request prior to issuing the final audit report. As stated in the above letter, appendices and the attached documents we think we have significant enough documentation to claim the auditors have incorrectly included several projects in their findings.

We would also like to note for the record that the audit of the Minneapolis EZ took place over 5 months utilizing 2 FTEs, while our response was required to be submitted in 15 calendar from December 11th which includes the Christmas holiday. With more response time, it's likely we would be able to provide more thorough documentation of the benefits to EZ residents.

The City of Minneapolis appreciates the time and effort spent by your staff in its review of our EZ program and trust that the final report will reflect our concerns noted here.

Sincerely,



Kim W. Havey

CC: Mayor R.T. Rybak
Council President Paul Ostrow
City Coordinator John Moir
HUD EZ/EC Director Pamela Glekas-Spring
HUD EZ/EC lead contact Lisa Hill
HUD MN CPD Director Alan Joles
Mpls. EZ Board Co-Chair Peter Heegaard
City of Minneapolis Finance Staff Terri Spencer

Attachments:

Appendix to 24 CFR Part 598
Appendix A, B and C responses to the project specific findings in the appendix to the draft audit
Near North Planning and Development HUD Implementation plan
Plymouth Christian Youth Center list of events and number of attendees
MN Public Radio article on the EZ investment in Public Schools Technology
Green Institute HUD 2002 annual report
Near North Phase IA and IB Sources and Uses
Park Plaza location documentation
Urban Ventures annual report narrative on Opportunity Kitchen
Hawthorne Homesteading new home addresses
Project Coordinator Job Description
MinnPERMS Scope of Services

**Response to Appendix A
Schedule of Ineligible Expenses**

The City of Minneapolis disagrees with this schedule of ineligible costs. As stated in the main text under the response to finding three, HUD approved this expenditure as a line item through the PERMS system and at no time did anyone at HUD indicate that this was not an appropriate area to charge this expense to. We have attached documentation to prove this point.

Based on this point we suggest that the IG amend their audit report recommendation 3A to state that the Near North Project cost category should be credited \$9,705 and EZ administration cost category be debited \$9,705 and to not list it at all in appendix A as an ineligible expense.

As part of our continued effort to more effectively manage the Minneapolis EZ and to ensure more accurate reporting and expensing a new project coordinator position has been created at the Minneapolis EZ. The position is expected to be filled by the end of January 2003. A copy of the job description is attached.

Response to Appendix B Individual Evaluations for the Projects Reviewed

- Plymouth Christian Youth Center
- Minneapolis Public Schools Wireless Technology
- Agape 24-Hour Childcare Development Center
- Green Institute
- Near North Phase IB
- Park Plaza
- Near North Planning and Development

Based on further documentation and explanation provided below the City of Minneapolis recommends that the following projects be removed from the findings: Plymouth Christian Youth Center, Green Institute and Park Plaza.

Plymouth Christian Youth Center:

The City of Minneapolis agrees that based on the documentation initially provided to the auditors by the implementing agency the number of people directly benefited may have been over stated for the reporting year. Attached is further information about programs at PCYC and their benefit to residents of the EZ. With over 2,000 neighborhood residents served it is estimated that at least 500 reside in the EZ (see attached).

It is also important to note that some of the addresses are not documented because addresses were not collected at all events. For example, at last year's PCYC gift sale in December 2001 there were over 800 children that participated with their families. Documentation of participants was not recorded in 2001, and therefore not provided to auditors. The Plymouth Christian Youth Center anticipated serving 900 children for the 2002 event and to improve management controls will be recording addresses to document the benefit to Empowerment Zone residents.

[At PCYC's annual Children's Gift Sale gifts are provided by individuals, churches and church youth groups, and businesses. The PCYC Capri Alternative School and Neighborhood Center is turned into a "store" for one day with thousands of high quality gifts for all ages. Every child is matched with an adult volunteer who guides them in making choices about the gifts they will give to family and friends.]

It should also be noted that the number of 500 people benefited could also be interpreted as an estimate based on the number of families members of each of the 88 children that live in the EZ (documented during the audit) and were served by the PCYC. The issue thus again arises as to who is considered a direct beneficiary?

As we move forward the Minneapolis EZ will adopt for this project the definition of a direct beneficiary as a student who is receiving an education at the PCYC school that was renovated with the assistance of EZ funding. For the purposes of the audit period the definition was much more broad to include all of the uses at the new building.

We would also like to make it clear that the Minneapolis EZ has implemented a performance based contracting system. In the case of PCYC the contract states that the \$175,000 EZ investment is a loan. \$100,000 may be forgiven by achieving goals that directly benefit EZ residents. In this case, a \$2,500 credit is charged against the loan for each EZ resident student who graduates from high school. PCYC has 5 years in which to maximize their credit. After five years whatever outstanding balance is left becomes due and payable to the EZ with interest. The loan is secured with a mortgage on their new building. Considering the fact that PCYC is an alternative school for students who have not functioned well in a traditional school setting, high school graduation for their students is no easy task. Moreover, it is clear from the contract that if the school can not show benefit to EZ residents they will have to pay back all the funds with interest and thus both HUD and the City of Minneapolis are securely protected from any risk associated with a lack of performance by PCYC. This is standard practice for the Minneapolis EZ.

Based on this information we are requesting that Plymouth Christian Youth Center be removed as a project under finding One.

To improve reporting accuracy the City is in the process of hiring a staff person who will be responsible for managing the EZ Projects and will be charged with the responsibility of monitoring and reporting on the progress of these projects. We expect to have that person in place by the end of January 2003. Please see that attached job description for further detail.

The City will also invest in project management software tailored specifically to fit the HUD required Performance Measurement System (PERMS). This will increase controls and assist staff in ensuring accuracy and oversight in the annual report. This new system will begin immediately. A scope of services for "MinnPERMS" is attached.

Minneapolis Public Schools Wireless Technology Project:

In this case we agree that Minneapolis incorrectly reported the exact number for one output for the Minneapolis Public School Wireless Technology project.

The EZ office did not verify the information presented by the Minneapolis Public Schools (MPS). It was determined for cost saving reasons that 1,728 names and addresses submitted by MPS of those who benefited could not have been checked to submit the annual report to HUD on time. Reviewing all addresses would not have been an efficient use of staff time. When the IG auditors did verify the addresses of the students who used the computers in 2001 and 2002, they found that 981 students had access to the technology. Thus significant benefit to EZ residents was achieved.

It should also be noted that as part of this investment in computers the EZ initiated a program called "Empowering Youth For Career Success," an e-mentoring program implemented by Achieve!Minneapolis. This program partners with corporations to provide e-mentors to public school students. More than 1,000 corporate employees and students are involved. Thus this program provides much more benefit to EZ residents than is even implied by the 981 students benefiting. For a June 2001 public radio report on the use of the technology go to: http://news.mpr.org/features/200106/04_pugmiret_computers/. A copy of the article is attached.

In the future, with the addition of a new staff person and the use of MinnPERMS, we will be monitoring the projects regularly and confirming that the outputs are reported accurately. However, we also need to work with HUD to determine a clearer definition of the term “benefiting resident.”

Agape 24-Child Development Center:

In this case, we are assuming that the IG did not feel that partnering programs are considered to operate in connection with a project. We agree that the number of programs operated by the implementing agency was over reported according to IG definitions. This was not due to a lack of verification, but instead a lack of a definition of what services can or can not be counted in annual reports. This was not an attempt to provide misleading information, but instead an attempt to show the entire scope of the program.

Agape Child Development Center is a program that provides 24-hour childcare. They do this in part because of their involvement with many individuals who suffer from domestic abuse. Thus they work with mainly women who have found themselves homeless as a result of being forced to leave an abusive environment. Oasis of Love and Agape works with them and their families and refers them to organizations that can provide housing and other services. So while the programs reported might not be operated in house by the implementing agency they are a well-known source of referrals and have numerous partnering agencies.

Therefore we feel that homeless residents were served and that this is subject to HUD’s interpretation of the regulations. Once the outputs and measurement are clearly defined, the City will communicate this to the project administrator and then these will be monitored by the new staff person that is expected to be in place by the end of January 2003.

Green Institute:

The City of Minneapolis committed EZ funds to guarantee a loan to the Green Institute. The purpose of the guarantee was to secure a loan for the Green Institute from Community Loan Technologies.

This project should be removed from the finding because EZ funds were not used and the implementing agency did not over report the number of EZ resident jobs created or retained.

Page 23 of the draft audit states that the City reported 20 residents jobs created or retained. This statement is incorrect. The City reported that 20 EZ resident jobs were projected to be created or retained, but that to date (at the time of the report) 5 jobs had been created or retained. When IG auditors reviewed the documentation they found that 9 EZ resident jobs were created or retained at the Green Institute and Minneapolis Transit Constructors. We are pleased that the actual benefit was even higher than initially reported.

It should be noted that although the information was slightly inaccurate (by 4 residents) it was under reported, not over reported. It should also be noted that this was a loan guarantee and that EZ funds leveraged private investment. No EZ funds were used or drawdown. The guarantee of the loan is no longer in place because the loan has been re-paid in full.

Based on this information we are requesting that the Green Institute be removed as a project from finding One.

However, as mentioned earlier the City is in the process of hiring a staff person who will be responsible for managing the EZ Projects and will be charged with the responsibility of monitoring and reporting on the progress of these projects. We expect to have that person in place by January 2003. MinnPERMS will also assist staff in tracking jobs created and retained to ensure that we accurately report the full benefit of the program.

Near North Phase IB:

Because of a data entry error the sources and uses for the Near North Phase IB Project were inaccurately reported. The correct list of sources for the project has been kept on file in the City's office and is attached to this appendix.

It is important to note that although there was a data entry error for this implementation plan the information for the total project was not over reported. The Minneapolis Public Housing approved a total of \$400,000 for Phase I (\$200,000 for IA and \$200,000 for IB).

The hiring of a new staff person and implementation of MinnPERMS will improve the accuracy of implementation plans.

Park Plaza:

The Park Plaza Project should be removed from the finding because the milestones were not inaccurately reported in June 30, 2001. All milestones for Park Plaza were reported as N/A in 2001 because an agreement between the City and implementing agency (MCDA) for the funds had not yet been executed.

It is important to note that HUD approval through PERMS is in place before an agreement (contract or Memorandum of Understanding) is entered into with a lead implementing agency for Empowerment Zone funds. For example, HUD approved an implementation plan for Park Plaza before the June 30, 2001 annual report was due, but the actual Memorandum of Understanding (MOU) and drawdown of funds for Park Plaza was not completed until after June 30, 2001. For this reason all milestones and outputs were recorded as N/A. It is also important to note that staff reported all milestones and outputs as N/A, not 0. The City reported the most accurate available information at the time of the report. The milestones and outputs were then reported on by the implementing agency for Park Plaza (the MCDA) in the 2002 annual report.

Also, the percentage of resident benefit not noted in the appendix, but referenced on page 8 of the draft audit should be changed from 7% to 100%. Park Plaza is a 134 unit project based HUD section 8 apartment complex located in the North Minneapolis EZ area. All of the five buildings are in the EZ and were renovated with the assistance of EZ funds. Please see the attached documentation noting the addresses (located in the EZ) of the buildings and the number of units (134).

Based on this information Park Plaza should be removed as a project from finding One.

The addition of a new staff person and the use of MinnPERMS will ensure timely reports.

Near North Planning and Development:

Regarding the project's outputs the City did under report the number of residents participating in community meetings for the planning of the Near North side. We did not think it was time and money well spent to verify the addresses of more than 500 people whom attended the numerous community and task force meetings. We are of course pleased to note that the auditors did confirm that of the hundreds who did participate in this multi year planning effort at least 354 were documented EZ residents.

The addition of a project coordinator staff position and MinnPERMS will allow the EZ to more effectively manage available documentation of resident participation so it is ready and available when annual reports are due.

Appendix C
Response to the projects listed in the chart under Finding Two

- Opportunity Kitchen
- Near North Phase IB
- Coliseum
- Park Plaza
- Plymouth Christian Youth Center
- Hawthorne Homesteading
- Agape 24-Hour Childcare Development Center

Based on further documentation and explanation provided below the City of Minneapolis recommends that the following projects be removed from the finding two: Near North Phase IB, Park Plaza, and Hawthorne Homesteading.

Opportunity Kitchen:

This is a commercial kitchen owned by Urban Ventures, Leadership Foundation - a faith based non-profit working in the South Minneapolis EZ. The kitchen is located in the EZ and is owned by Urban Ventures, but run by the Minneapolis-St. Paul Food Shelf network now called Second Harvest. It is their main commercial kitchen in the Twin Cities. It is their goal to prepare 2,000 meals a week for needy families. It is the goal of the Minneapolis EZ to use this kitchen to provide training for difficult to employ EZ residents in food handling. It is based on the D.C. Kitchen model. The auditors report that this new kitchen served no one. But what is not noted is that the kitchen has only been operating since October 2001 and they have only had two pilot training classes as of June 30, 2002. The IG auditors also did not consider anyone who received a meal prepared at the kitchen to be a beneficiary.

It was also omitted that the funding provided to Urban Ventures is in the form of a five-year performance based contract. The funding is provided in the form of a loan that is partially forgiven at the rate of \$2,500 per EZ resident who receives a certificate in food handling and is employed at \$10/hour for one year. The EZ director must sign off on these requests so the addresses are verified. Urban Ventures is making current interest payments on the loan, the loan is being serviced at no cost to the Minneapolis EZ by Wells Fargo Bank and is secured by a mortgage on Urban Ventures real estate. If no EZ residents benefit directly the loan is due and payable in full with interest.

We believe that the audit should include reference to the fact that the Minneapolis EZ has gone above and beyond the federal requirements to ensure that if EZ residents are not benefited as stated in the application for funding that funding will be due back to the EZ with interest and is collateralized by real estate.

Near North Phase IB:

This funding was provided in the form of a predevelopment loan. This means funding was provided to the developer to cover the cost of architects and engineers prior to the development of new housing and infrastructure. Thus again the reporting is not simple. Who benefited from this can be construed to be all the residents who have moved into the new public and affordable

housing or no one as the IG contends. No individual served or benefited is not true. At the time of the closing of this contract and the payback of the loan no one had yet moved into the housing because it was not yet built. As of November 1, 2002 there are 10 families who have moved into the public housing in phase IB. More than 100 more will be moving in by February 1, 2003 and more than 700 by the time all four phases of the 73-acre redevelopment are completed.

It should also be noted that the Near North redevelopment is in the EZ and part of a lawsuit settlement against HUD known as Hollman vs. Cisneros. There is a requirement to provide the new housing in a timely manner and the support of the EZ has been critical to meeting these deadlines. Also, it should be noted that this funding was paid back with interest.

Based on this information we are requesting that Near North Phase IB be removed as a project under finding Two.

Coliseum:

In this case the IG is contending that only 65 individuals were served and 2 EZ residents benefited. What they are counting is the number of EZ people employed at CLUES and La Clinica, two tenants of the building. There are several other tenants including a Denny's restaurant whose employee addresses was not reviewed.

It is our contention that many more EZ residents benefited from the renovation of the coliseum building than the IG noted. We are currently collecting information on all the people who have received service from the tenants. Knowing that La Clinica is providing health care services mainly to Spanish speaking residents and knowing that CLUES is the largest non-profit organization serving Latino people in the state of MN and that according to the 2000 census 17% of the South Minneapolis EZ considers themselves Latino we believe that the number of EZ residents served is much greater than is listed in the audit.

It should also be noted that this funding was provided in the form of a loan. Funding will be repaid and re-leveraged when interest and principle repayments begin in 2005.

Park Plaza:

This was discussed earlier in response to recommendation number two of finding two. I will repeat our response here for the ease of the readers.

The auditors state that only one Empowerment Zone resident is served at Park Plaza. We believe this only counts the number of EZ residents who were hired by the construction contractors to renovate the buildings and does not take into consideration the number of EZ residents who reside in the building. Park Plaza is a 134 unit project based HUD section 8 apartment complex located in the North Minneapolis EZ. All of the five buildings are in the EZ and were renovated with the assistance of EZ funds. In our opinion all the families residing in the 134 units of housing are EZ residents and have benefited from the EZ investment used to renovate the buildings. Therefore, it should be reported that 100% of the benefit of this project accrued to EZ residents.

Based on this information we are requesting that Park Plaza be removed as a project under finding Two. Documentation showing that 100% of the Park Plaza benefit went to Empowerment Zone residents is attached.

Plymouth Christian Youth Center (PCYC):

In this case again the definition of benefit is needed to clarify who is considered to be benefiting. The total number of individuals served and residents benefited is based on the number of students attending the school. It does not include all the organizations and other area business people and residents who benefited from the new building. As an attachment we have included a list of the number of people who attended various community events in the new PCYC building. Should they be counted, we think so. Thus making the contention that only 90 EZ residents benefited invalid.

It should also be noted that again we established a performance-based contract with PCYC. PCYC may have \$100,000 of their \$175,000 loan forgiven over the next 5 years at the rate of \$2,500 per EZ resident student they help graduate with a diploma from high school. Considering the Minneapolis Public Schools graduation rate of 58% this is no easy task.

Here again it should be noted that the Minneapolis EZ has gone above and beyond the minimum to ensure that benefit is received by EZ residents. At the end of the contract if this has not happened all the funding is paid back with interest. There is no down side risk for HUD or the City.

Hawthorne Homesteading Program:

The intent of this project is to infill vacant lots in the Hawthorne neighborhood with new single family homes. More than 200 vacant lots exist in this neighborhood. Leveraging other private and public funds a total of 42 homes have been built over the last two years. With the Minneapolis EZ committing to fund 6 homes. The IG auditors state in this finding that only 2 EZ residents were served. It is our understanding that this is the number of homes that were built by June 30, 2002 when the annual report was due. In the EZ contract, the \$200,000 was intended to help 6 families move into new homes in the EZ. That was achieved this year, but was done for less money than initially budgeted. Therefore, the contract has been extended through 2003 and 2 more homes will be built and sold to families in the EZ in Spring 2003.

Since every one of the homes built with EZ funds is located in the EZ it is our contention that 100% of the benefit accrued to EZ residents. Based on this information we are requesting that Hawthorne Homesteading be removed as a project under finding Two. Documentation showing the list of addresses of the new homes in the EZ is attached.

Agape 24-hour childcare Development Center:

This project is the first 24-hour 7 day a week daycare in Minneapolis. It is located in North Minneapolis along a bus route that makes it convenient for 2nd and 3rd shift parents who work at North Memorial hospital to drop off and pick their kids up. It is also a safe haven for victims of domestic abuse who find themselves homeless and need help providing care for their children.

While we can not contend that the number of EZ residents served is 53, it should be noted that, like all of the audit's finding, it is based on a snapshot in time. For the period audited, 53 of 200 individuals served were EZ residents. We have a 5-year contract with Agape and thus the number of EZ residents benefited will increase in real numbers and quite possible in the percentage of individuals served over time.

Attachments

1. Near North Planning and Development HUD Implementation Plan
2. Plymouth Christian Youth Center – summary of programs and participants
3. Minnesota Public Radio article – June 2001
4. Near North Phase IA and IB Sources and Uses
5. Park Plaza Documentation (addresses, map, 11/18/02 memorandum)
6. Urban Ventures Opportunity Kitchen Annual Report Narrative
7. Hawthorne Homestead Project Addresses
8. Project Coordinator Job Description
9. MinnPERMS Scope of Service

Distribution

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