
AUDIT REPORT



CITY OF CARMEL ECONOMIC DEVELOPMENT INITIATIVE – SPECIAL PURPOSE GRANT (B-02-SP-IN-0220)

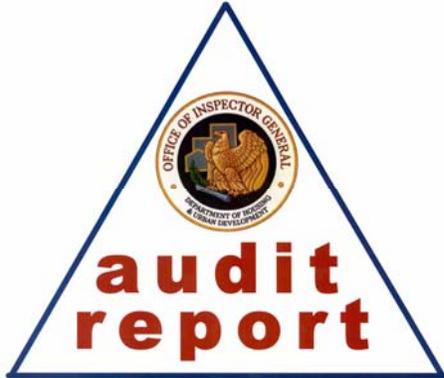
CARMEL, INDIANA

HUD's Interest in \$1 Million in Grant Funds Awarded to the
City Was Not Secured

2005-CH-1019

SEPTEMBER 28, 2005

OFFICE OF AUDIT, REGION V
CHICAGO, ILLINOIS



Issue Date	September 28, 2005
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Audit Report Number	2005-CH-1019
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TO: Francis P. McNally, Director of Congressional Grants, DECC

FROM: 
Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: HUD's Interest in \$1 Million in Economic Development Initiative – Special Purpose Grant Funds Awarded to the City of Carmel Was Not Secured; Carmel, Indiana

HIGHLIGHTS

What We Audited and Why

We audited the City of Carmel, Indiana's (City) Economic Development Initiative - Special Purpose Grant (Grant). We initiated the audit in conjunction with our internal review of the U.S. Department of Housing and Urban Development's (HUD) oversight of Economic Development Initiative – Special Purpose Grants. The review is part of our fiscal year 2005 annual audit plan. We chose the City's Grant based upon a statistical sample of fiscal years 2002 and 2003 Economic Development Initiative – Special Purpose Grants, in which 90 percent or more in funds were disbursed. Our objectives were to determine whether the City used its Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted property.

What We Found

The City used the Grant funds in accordance with HUD's requirements. It used \$1 million in Grant funds to pay for the area wide subterranean detention system and reflecting pool design of Veterans Plaza and the Reflecting Pond. However, it did not place a covenant on the property title for Veterans Plaza and the Reflecting Pond, assuring nondiscrimination based on race, color, national origin,

or handicap. Further, HUD did not request the City to record HUD's interest on the property title for Veterans Plaza and the Reflecting Pond.

What We Recommend

We recommend that HUD's director of congressional grants require the City to record a covenant on the title assuring nondiscrimination based on race, color, national origin, or handicap and record a lien on the property title for Veterans Plaza and the Reflecting Pond showing HUD's interest in the assisted property. If the covenant and lien are not recorded, the City should reimburse HUD \$1 million from nonfederal funds for the Grant funds used to pay for the area-wide subterranean detention system and reflecting pool design of Veterans Plaza and the Reflecting Pond.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided our discussion draft audit report to the City's director of administration and HUD's staff during the audit. The director of administration declined our offer for an exit conference.

We asked the director of administration to provide comments on our discussion draft audit report by September 17, 2005. The director of administration provided written comments dated September 16, 2005. The director of administration agreed to implement corrective action to address our finding. The complete text of the written comments can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Economic Development Initiative program. The U.S. Department of Housing and Urban Development's (HUD) Economic Development Initiative program includes noncompetitive Economic Development Initiative – Special Purpose Grants. HUD awards Economic Development Initiative – Special Purpose Grants to entities included in the U.S. House of Representatives' conference reports.

The City of Carmel, Indiana. Organized under the laws of the State of Indiana, the City is governed by a mayor and seven-member council. The U.S. House of Representatives' Conference Report 107-272 set aside \$1 million in Economic Development Initiative – Special Purpose Grant (Grant) funds to the City for its Indiana parks development. In August 2002, HUD awarded the City the \$1 million Grant to pay for the first two phases of the park effort, including the establishment of a reflecting pool feature and an area-wide subterranean detention system, respectively. The City's Department of Administration administers the Grant. The City's records for the Grant are maintained at Carmel City Hall, located at One Civic Square, Carmel, Indiana.

We initiated this audit in conjunction with our internal review of HUD's oversight of Economic Development Initiative – Special Purpose Grants. The review is part of our fiscal year 2005 annual audit plan. We chose the City's Grant based upon a statistical sample of fiscal years 2002 and 2003 Economic Development Initiative – Special Purpose Grants, in which 90 percent or more in funds were disbursed.

Our objectives were to determine whether the City used its Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted property.

RESULTS OF AUDIT

Finding: HUD's Interest in \$1 Million in Grant Funds Awarded to the City Was Not Secured

The City used \$1 million in Grant funds to pay for the area-wide subterranean detention system and reflecting pool design of Veterans Plaza and the Reflecting Pond; however, the City did not place a covenant on the property title for Veterans Plaza and the Reflecting Pond assuring nondiscrimination based on race, color, national origin, or handicap. Further, HUD did not request the City to record HUD's interest on the property title for Veterans Plaza and the Reflecting Pond. The City did not record the covenant on the title because it lacked effective oversight over applicable Grant requirements. As a result, HUD's interest in Veterans Plaza and the Reflecting Pond are not protected.

The City Used \$1 Million in Grant Funds without Placing a Covenant on the Title to Ensure Nondiscrimination

Contrary to federal requirements, the City did not secure HUD's interest in \$1 million in Grant funds used to pay for the area-wide subterranean detention system and reflecting pool design of Veterans Plaza and the Reflecting Pond. The funds were disbursed from September 2002 through December 2003. The City failed to place a covenant on Veterans Plaza and the Reflecting Pond's property title to assure nondiscrimination based on race, color, national origin, or handicap. The purpose of the covenant is to ensure nondiscrimination during the period in which Veterans Plaza and the Reflecting Pond are used as outlined in the City's application for the Grant or for another purpose involving similar services or benefits. The recording of the covenant will provide HUD recourse if discrimination based on race, color, national origin, or handicap occurs in relation to Veterans Plaza and/or the Reflecting Pond.

HUD's Interest in Veterans Plaza and the Reflecting Pond Is at Risk

The City's director of administration said he did not believe that costs for developing the area-wide subterranean detention system and the reflecting pool design qualified as acquiring real property. However, funds used to develop land and design structures does fall within the regulatory meaning of real property as outlined in 24 CFR [*Code of Federal Regulations*] 1.5 and 8.50. The recording of

the covenant will provide HUD recourse if discrimination based on race, color, national origin, or handicap occurs in relation to Veterans Plaza and/or the Reflecting Pond.

HUD Did Not Request the City to Record HUD's Interest on the Title for Veterans Plaza and the Reflecting Pond

HUD did not request the City to record HUD's interest on the property title for Veterans Plaza and the Reflecting Pond. The recording of HUD's interest in the assisted property will help protect HUD in case the property is sold or is no longer used for its intended purpose. The City's director of administration certified in Standard Form 424D, Assurances – Construction Programs, section 3, that the City would record the federal interest in the title of real property in accordance with awarding agency directives.

HUD's Office of Congressional Grants' position is that Standard Form 424D only requires the City to record HUD's interest in Veterans Plaza and the Reflecting Pond if HUD issued a directive that requires applicants to record HUD's interest in real property or HUD specifically directs the City to record HUD's interest in Veterans Plaza and the Reflecting Pond. HUD did not issue any directives requiring grant recipients to record HUD's interest in real property or specifically direct the City to record HUD's interest. However, HUD clearly has the authority to require a grantee to record HUD's interest in an assisted property. Therefore, HUD's interest in Veterans Plaza and the Reflecting Pond is not protected in case the property is sold or is no longer used for its intended purpose.

Recommendations

We recommend that HUD's director of congressional grants require the City to

- 1A. Record a covenant on the title assuring nondiscrimination based on race, color, national origin, or handicap and record a lien on the property title for Veterans Plaza and the Reflecting Pond showing HUD's interest in the assisted property. The covenant and lien should help ensure that the City protects HUD's interest in the \$1 million in Grant funds for Veterans Plaza and the Reflecting Pond.
- 1B. Reimburse HUD from nonfederal funds for the Grant funds used to pay for the area wide subterranean detention system and reflecting pool design if the covenant and lien are not recorded.

SCOPE AND METHODOLOGY

We performed the audit at the City's administrative offices and its City Center in July 2005. To accomplish our objectives, we interviewed HUD's staff and the City's employees.

To determine whether the City used Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted property, we reviewed

- U.S. House of Representatives' Conference Report 107-272,
- HUD's file related to the Grant,
- The City's financial records, and
- The City's website for organizational information on the City.

We also reviewed 24 CFR [*Code of Federal Regulations*] parts 1, 8, and 85; 56 *Federal Register* 16337; 70 *Federal Register* 35967; HUD Directives 1.5, 8.50, and 85.31; Office of Management and Budget Circulars A-21, A-87, A-110, and A-122; and HUD Handbook 2000.06, REV-3.

The audit covered the period from August 1, 2002, through June 10, 2005. This period was adjusted as necessary. We performed our audit in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

- Effectiveness and efficiency of operations,
- Reliability of financial reporting,
- Compliance with applicable laws and regulations, and
- Safeguarding resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined the following internal 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.

A significant weakness exists if internal controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weakness

Based on our audit, we believe the following item is a significant weakness:

- The City did not record the covenant on the title because it lacked effective oversight over applicable Grant requirements.

APPENDIXES

Appendix A

SCHEDULE OF FUNDS TO BE PUT TO BETTER USE

Recommendation number	Funds to be put to better use 1/
1A	<u>\$1,000,000</u>
Total	<u>\$1,000,000</u>

1/ “Funds to be put to better use” are quantifiable savings that are anticipated to occur if an Office of Inspector General (OIG) recommendation is implemented, resulting in reduced expenditures at a later time for the activities in question. This includes costs not incurred, deobligation of funds, withdrawal of interest, reductions in outlays, avoidance of unnecessary expenditures, loans and guarantees not made, and other savings.

AUDITEE COMMENTS



JAMES BRAINARD, MAYOR

September 16, 2005

**VIA FACSIMILE and
FEDERAL EXPRESS DELIVERY**

Mr. Brent Bowen
Assistant Regional Inspector General For Audit
United States Department of HUD-Office
of Inspector General
77 West Jackson Blvd., Suite 264
Chicago, IL 60604

Re:

Dear Mr. Bowen:

This letter is sent to you on behalf of the City of Carmel (the "City") in response to the draft audit report number 2005-CH-101X (the "Draft Report") prepared for the Economic Development Initiative Special Purpose Grant (B-02-SP-IN0220) (the "Grant") which was awarded to the City of Carmel. The City reserves the right to supplement this response.

Our comments to the Draft Report are as follows:

1. **Highlights (pages 1 and 2).** Each of these items is discussed in greater detail in other areas of the Draft Report and we will comment on them in the remainder of this letter.
2. **Background and Objectives (page 3).** The City has no information to comment on this section other than the City agrees with the facts set forth in the second paragraph.
3. **Results of Audit (pages 5 and 6).** The City acknowledges that it has not recorded a covenant on the Veterans Plaza and Reflecting Pond property (the "Property") regarding nondiscrimination. The City agrees that HUD has never directed the City to record HUD's interest in the Property. The City does not agree with the Finding that the City lacked effective oversight of the Grant.

ONE CIVIC SQUARE, CARMEL, IN 46032 OFFICE 317.571.2401, FAX 317.844.3498
EMAIL jbrainard@ci.carmel.in.us

Mr. Brent Bowen
September 16, 2005
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Our response to the Recommendations are as follows:

- 1A. The City agrees to cause a covenant to be recorded on the Property which provides that the City will not discriminate based on race, color, national origin, or handicap with respect to its use of the Property. Such covenant shall be recorded within the next 60 to 90 days.

The City agrees with the finding that HUD has never directed the City to record a lien on the Property to protect HUD's interest therein. The City requests that HUD provide further information regarding the purpose of this lien. Based on the City's review of the relevant documents, it appears that this obligation to record the Federal interest in the Property arises from paragraph 3 of the Assurances - Construction Program, which is part of the Grant Application. This paragraph states that the purpose of such recording is to prevent the disposal, change in use or other change in title of the Property without HUD's permission or instruction. Upon receipt of such information and a directive from HUD, the City will finally determine whether it is required to record such a lien. If such recording is required, the City will commit to cause the lien to be recorded within 60 to 90 days after such directive and determination are made.

- 1B. Given the City's willingness to comply with the foregoing recommendations, it is not necessary to provide for reimbursement to HUD of any Grant funds.

It is our understanding that, upon your receipt and review of this response, you will contact the City for further information or clarification prior to the filing of a final report. Please contact me as soon as possible if this is not correct. Also, please direct all correspondence regarding this matter to me at One Civic Square, Carmel, Indiana 46032, (317) 571-2403.

Sincerely,


Steve Engelking
Director of Administration
City of Carmel

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Appendix C

FEDERAL REQUIREMENTS

The City's grant agreement with HUD, article I, section B, states the grants funds must be made available in accordance with 24 CFR [*Code of Federal Regulations*] parts 1 and 8. Section E of article I states the City will comply with 24 CFR [*Code of Federal Regulations*] part 85.

According to 24 CFR [*Code of Federal Regulations*] 1.5(a)(2), in the case of real property, structures, improvements thereon, or interests therein, acquired through a program of federal financial assistance, the instrument effecting any disposition by the recipient of such real property, structures, improvements thereon, or interests therein shall contain a covenant running with the land assuring nondiscrimination based on race, color, or national origin for the period during which the real property is used for a purpose for which the federal financial assistance is extended or for another purpose involving the provision of similar services or benefits.

According to 24 CFR [*Code of Federal Regulations*] 8.50(c)(2), when no transfer of property is involved, but property is purchased or improved with federal financial assistance, the recipient shall agree to include a covenant in the instrument effecting or recording any later transfer of the property for the period during which it retains ownership or possession of the property to assure nondiscrimination based on a handicap.

HUD Directive 85.31 and 24 CFR [*Code of Federal Regulations*] 85.31 state title to the real property shall vest in the recipient as long as the recipient uses the real property for its authorized purpose and does not encumber the real property without HUD's approval. Section 85.31(c) states when the real property is no longer needed for the authorized purpose, the recipient shall request disposition instructions from HUD. HUD shall require the recipient to do the following: (1) retain title to the real property without further obligation to the federal government after it compensates the federal government the percentage of the current fair market value of the real property attributable to the federal participation in the project; (2) sell the real property and compensate the federal government for the percentage of the current fair market value of the real property attributable to the federal participation in the project; or (3) transfer title to the real property to the federal government or to an eligible third party and be entitled to compensation for its percentage of the current fair market value of the real property.

According to 56 *Federal Register* 16337, "directive" means a handbook (including a change or supplement), notice, interim notice, special directive, and any other issuance that the department may classify as a directive.

The City's director of administration certified in Standard Form 424D, Assurances – Construction Programs, section 3, that the City would record the federal interest in the title of real property in accordance with awarding agency directives and would include a covenant in the title of real property acquired in whole or in part with federal assistance to assure nondiscrimination during the useful life of the project.