



U. S. Department of Housing and Urban Development

*New York/New Jersey Office
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**Office of Inspector General
Office of Audit**

November 15, 1996

Audit Related Memorandum No. 97-NY-243-1801

MEMORANDUM FOR: Michael Merrill, Director, Community Planning and Development
Division, Buffalo Area Office

FROM: A. Paul Kane, District Inspector General for Audit,
New York/New Jersey

SUBJECT: UDAG and Small Cities Programs
City of Hudson, New York

We have completed a review of the UDAG and Small Cities programs administered by the City of Hudson, New York (Grantee). The primary objective of the review was to address concerns raised by the U.S. Department of Housing and Urban Development's (HUD) Office of Economic Development Division in Washington, DC. The concerns relate to a proposed UDAG prepayment arrangement between the Grantee and L & B Contract Industries, Inc., the recipient of Urban Development Action Grant (UDAG) No. B-85-AB-36-0603. Additionally, we reviewed selected Small Cities transactions for any indications of possible improprieties or noncompliances with HUD regulations.

Our review disclosed that the proposed UDAG prepayment terms conflict with the UDAG agreement. Further, the Grantee entered into agreements with the recipient that are not allowed, or specified in the UDAG agreement, or approved by HUD.

Additionally, the review disclosed weaknesses in the Grantee's internal controls and procedures related to the procurement of services and possible conflicts of interest. We are bringing these matters to your attention so that effective administrative actions can be taken to address and correct the weaknesses.

BACKGROUND

The Small Cities Program is administered by the Hudson Community Development and Planning Agency (HCDPA). The UDAG programs are administered by the Hudson Development Corporation (HDC). Both entities are located at 444 Warren Street, in Hudson, New York. The Executive Director of HCDPA is Ann Vedder and HDC's Executive Director is Jayme B. Lahut.

The HCDPA administered \$2,567,500 in Small Cities Grants received between 1989 and 1993. Although the HDC administered several UDAGs during the period, we only reviewed UDAG No. B-85-AB-36-0603 in the amount of \$556,000.

The results of our review were discussed with Grantee and Subrecipient officials during our site work, and in an exit conference held on August 29, 1996.

REVIEW RESULTS

Grantee Executed a UDAG Prepayment Agreement and Subordinated the UDAG Lien Without HUD's Knowledge or Approval

The March 7, 1996, letter to you from HDC's legal counsel discloses four irregularities that were discovered by the new staff of HDC. The irregularities pertain to UDAG No. B-85-AB-36-0603, and are as follows:

1. There is an executed agreement between HDC and the Recipient (L & B) that permits the Recipient to repay the \$550,000 UDAG Note at any time after May 8, 1996, by paying only a present value amount of \$4,998.25.
2. The prepayment agreement is dated May 8, 1991, the same date as the UDAG Note.
3. HDC can find no evidence that the prepayment agreement was approved by the HDC Board, the Grantee or HUD.
4. L & B has not made any of the interest only payments required by the UDAG Note.

The results of our review show that the irregularities reported to you by the HDC's counsel have merit. In addition, we found that in February 1995, the HDC signed a subordination agreement with OnBank & Trust Co. subordinating the UDAG lien position for \$3,000,000 in new debt. Again, HUD was not informed of the subordination as required since the new debt may violate provisions of the UDAG Agreement.

Currently, the Grantee is seeking to amend the UDAG agreement. We reviewed a draft memorandum addressed to the Assistant Secretary of Community Planning and Development requesting that HUD

allow the Grantee to accept five years of back interest (\$137,500) as payment in full on the \$550,000 loan. As a justification for the amendment, the Grantee refers to continuing financial obligations due L & B by the City for public improvements apart from the UDAG. The City should be reminded that City obligations that are not a part of the UDAG activity are not necessarily the responsibility of HUD.

Weaknesses in Controls Affecting Small Cities Grants

Controls implemented by HCDPA do not always ensure that potential conflicts of interests are evaluated, that procurement activities are based on free and open competition, or that expenditures are reasonable.

Possible Conflicts of Interest and Procurement Weaknesses

- a. HCDPA's Executive Director is simultaneously employed by the National Development Council (NDC). Since NDC provides services to other communities that involve HUD funded activities, we believe that the dual position should be evaluated to ensure that it does not pose a conflict of interest.
- b. An HDC Board member has been hired to do HCDPA's secretarial work as an independent contractor without any competitive proposal process. The Board member is paid at an hourly rate of up to \$22. Payments from April 1995 through July 1996, totaled \$4,330.29.
- c. HCDPA's Executive Director awarded a consulting contract to the spouse of a Board member without competition. The contract has resulted in payments amounting to \$43,404.19, at hourly rates of up to \$170.
- d. HCDPA's Rehabilitation Specialist noncompetitively awarded rehabilitation work to a company owned by his brother. Payments to date total \$27,007.92.

Apart from the above, our test of expenditures disclosed one questionable disbursement of \$2,400 to a public relations firm for unspecified "public relations duties". We believe that the expenditure does not meet the required program objectives. Additional details on this matter are available upon request.

We are bringing these matters to your attention so that effective administrative actions can be taken to address and correct the weaknesses. We recommend that you remind the Grantee and Subrecipients of their responsibility to administer programs in accordance with pertinent regulations of the UDAG and Small Cities Programs.

Please contact us if you or your staff have any questions, or require copies of pertinent working papers. Also, please furnish us with copies of any correspondence issued related to this review.

Distribution

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