

# EXAMPLE OF A GRANTEE MONITORING LETTER TO A SUBRECIPIENT



August 9, 2021

Ms. Jane Brown  
Executive Director  
Midtown Community Development Corporation, Inc. (MCDC)  
606 Main Street  
Midtown, California

RE: Monitoring of MCDC's CDBG Activities

Dear Ms. Brown:

On July 21 and 22, 2021, [Name(s) of Monitor(s)], Monitoring Specialists for the Midtown Office of Community Development, monitored the MCDC's CDBG activities. The MCDC is a subrecipient of the City of Midtown and is carrying out two CDBG-funded programs: an economic development loan program and a housing rehabilitation loan and grant program. The economic development loan program provides financing for both existing and start-up businesses and funds a variety of business needs such as real estate, equipment, inventory, leasehold improvements, and working capital. The housing rehabilitation program assists primarily owner-occupied, low- and moderate-income housing in the East End neighborhood.

The period under review was from July 1, 2021 to June 30, 2021. In addition to examining relevant files in the course of the review, the Monitoring Specialists met with you, the MCDC Finance Director (Jane White), and the MCDC program directors for the economic development and housing rehabilitation programs (Bill Blue and Yvonne Grey, respectively). Monitoring Specialists also visited two assisted projects/cases for each program. An exit conference was held with you and your staff at the MCDC offices on July 22, 2021, to discuss the results of the monitoring.

The purpose of a monitoring visit is to determine whether the subrecipient has implemented and administered CD-BG-funded activities according to applicable Federal requirements. In this monitoring review, particular attention was paid to compliance with eligibility and National Objective requirements. Other areas emphasized were financial management systems, procurement practices, compliance with civil rights requirements, and use of program income.

Overall, the MCDC is making diligent efforts to comply with applicable Federal requirements. The Monitoring Specialists found that the MCDC had achieved significant improvements in their financial management systems and management of program income. During the previous monitoring visit, these two areas had been the source of several serious findings regarding inadequate internal controls and failure to keep proper records on receipt and use of program income. The most recent review, however, revealed that the MCDC's systems and procedures in these areas are now satisfactory. In fact, the MCDC's new bookkeeping system for tracking and reporting on the use of program income, with its automated generation of monthly reconciliations and reports, is exemplary. This office will be recommending its adoption by several other subrecipients in our community.

As a result of this most recent review, we are making two new findings and one concern regarding the use of CDBG funds. A *finding* is defined as a program element that does not comply with a Federal statute or regulation, whereas a *concern* is either a potential finding or a program weakness that should be improved to avoid future problems. The findings and concern are detailed below:

## **Finding Number 1—Public Benefit Requirements for Economic Development Loans**

24 CFR 570.203 of the CDBG regulations provides that CDBG funds may be used to assist a for-profit business, provided the grantee ensures that the appropriate level of public benefit will be derived before funds are obligated for that purpose. In the case of your economic development loan program, this means that a minimum number of full-time equivalent (FTE) jobs must be created or retained for each business assisted, in relation to the amount of CDBG funds

being provided to the business. Moreover, in order to ensure that the assistance provided does not unduly enrich the business, the subrecipient is expected to perform basic financial underwriting of each potential loan to determine that the amount of the contemplated financial assistance is not excessive, taking into account the actual needs of the business in making the project financially feasible. Therefore, a CDBG grantee must review a subrecipient's files for documentation demonstrating that both of these requirements are being met.

The recent review revealed that at least some of MCDC's project files lack sufficient documentation to demonstrate that basic financial underwriting was conducted. Three loans were reviewed in our sample of the files: No-Pest Termite Control, Sportsworld, and New Day Bakery. The files contained financial statements from each business. However, other documentation was not found to indicate that a financial analysis was conducted, and a determination made that the level of assistance provided was appropriate. There was also a lack of information that would demonstrate that the number of FTE jobs to be created by these businesses will meet the public benefit standards (i.e., that no more than \$35,000 per FTE job to be created was being provided to each business).

### **Corrective Action**

MCDC must provide documentation to demonstrate that, for each of these loans listed above, a financial analysis was conducted and a determination made that the level of loan provided was appropriate given the circumstances and that a determination was made that the public benefit limit mentioned above would be met, given the number of jobs expected to materialize. This documentation must be provided to the City of Midtown within thirty (30) days of the receipt of this letter. MCDC must also certify to this office that each of the remaining project loan files contains the documentation missing from these three case files. Lastly, for the next two loans, MCDC is requested to submit documentation supporting these two requirements (financial underwriting and public benefit) to our office for review in advance of loan approval.

### **Finding Number 2—Program Benefit from Economic Development Loans**

24 CFR 570.200(a) of the CDBG regulations requires that each activity assisted with CDBG funds meet one of the three National Objectives. Each provision of assistance to a for-profit business is considered a separate activity; therefore, each business so assisted with CDBG funds must meet a National Objective, and each loan file must contain relevant documentation to that effect. The MCDC has indicated that its economic development loans will meet the National Objective of principal benefit to low- and moderate-income persons through the creation of jobs for low- and moderate-income persons, and 24 CFR 570.506(b)(5) sets forth the requirements for documentation of the National Objective in such cases.

The July 2021 monitoring visit revealed, however, that some MCDC economic development loan project files (cases number A-13, A-17, and A-18) lack the necessary documentation to demonstrate that a National Objective has been met through the creation of jobs, per [24 CFR 570.506\(b\)\(5\)](#).

### **Corrective Action**

MCDC must provide this office with documentation regarding the creation of jobs for loans number A-13, A-17, and A-18. The documentation should include an accounting of the actual number of full-time equivalent positions created, by title, and the number of positions filled by low- and moderate-income persons. For each low- and moderate-income person hired, MCDC must also identify the method used to determine family income prior to the person's being hired, e.g., the Private Industry Council (PIC) referral or copies of the self-certification. If a self-certification is used, it must be signed by the employee and clearly advise that the information may be subject to verification.

Secondly, for all future activities, MCDC must assure this office that a system is in place to maintain documentation for a National Objective for each provision of assistance to a for-profit business.

Lastly, we advised the MCDC staff to provide language in its written loan agreements that would impose consequences upon any business failing to demonstrate a good faith effort in hiring the necessary percentage of low- and moderate-income persons.

### **Concern Number 1—Compliance with the escrow account requirements set forth in 24 CFR 570.511**

The above-referenced regulation sets forth four basic requirements for the use of escrow accounts:

1. The use of escrow accounts is limited to loans and grants for the rehabilitation of primarily residential properties containing no more than four units each.

2. An escrow account shall not be used unless the contract between the property owner and the contractor selected to do the rehabilitation work specifically provides that payment to the contractor shall be made through an escrow account.
3. All funds withdrawn under this section shall be deposited into one interest-earning account with a financial institution.
4. The amount of funds deposited into an escrow account shall be limited to the amount expected to be disbursed within 10 working days from the date of deposit.

Although the MCDC housing rehabilitation program has been able to meet these requirements thus far, a proposed change in the structure, staffing level, and procedures of the MCDC's Finance Office has raised some concerns about the continued ability of MCDC to achieve the 10-day standard for disbursement of escrow account funds.

**Requested Action**

We request that MCDC, within thirty (30) days of receipt of this letter, forward a detailed description of the proposed MCDC Finance Office re-organization that will reassure this office that there will continue to be a capacity to disburse escrow account funds within ten working days.

We look forward to receiving your responses within thirty (30) days of receipt of this monitoring letter by MCDC. If there should be any reason why your organization would have difficulty responding by this deadline, please contact me immediately.

We should add that the findings from our review, in our view, do not reflect negatively on MCDC's staff and their dedication to ensuring the success of the referenced programs. As previously mentioned, this office's Monitoring Specialists saw ample evidence of significant improvements that have been made by MCDC over the last year in the operations of its two CDBG-funded programs.

Monitoring Specialists appreciated the MCDC staff's continued assistance throughout the monitoring visits.

Sincerely,

[Name of Monitor]

[Title]

Midtown Office of Community Development