Ms. Leslye Krutko  
Director  
Housing Department  
City of San Jose  
200 East Santa Clara Street, 12th Floor  
San Jose, CA 95113-1905

Subject: Results of Program Monitoring  
Community Development Block Grant Program:  
B05-MC-06-0021 & B06-MC-06-0021

Dear Ms. Krutko:

The purpose of this letter is to report the results of our programmatic monitoring review of the City of San Jose’s Community Development Block Grant (CDBG) Program, conducted during the dates of August 28-30th and September 5th, 2007, by Rafael Cedillos, Sr. Community Planning and Development Representative.

The review covered the CDBG allocations for Program Years 2005-06 and 2006-07. The principal purpose of the review was to assure compliance with applicable CDBG Program regulations, statutory requirements, as well as provide any necessary technical assistance to City staff to improve program progress and effectiveness.

The Housing Department began to administer the CDBG Program during the Summer of 2006 upon transfer of the program from the Neighborhood Services Division of the Parks, Recreation and Neighborhood Services Department. The administration and operation of the program was determined to be highly efficient overall and accomplishments were consistent with respective annual action plans and reporting submissions to HUD, as well as the City’s five-year Consolidated Plan.

We highlighted the following outstanding features of the administration of the CDBG Program:

- Although limited in staff resources, the Housing Department has performed a commendable job in incorporating and implementing the City’s $12 million dollar annual CDBG Program into its internal structure in a relatively short period of time. We also observed that staff are highly proactive, diligently research eligibility and other program requirements and policy, and consult with HUD as may be necessary, to address specific issues and questions pertaining to projects and activities funded under the CDBG program.
• An updated Policies and Procedures Manual was very comprehensive covering all aspects of the program’s administration and implementation, including HUD financial standards.

• The documentation contained in sub-recipient grant files and housing rehabilitation project files was well organized, consistent and complete. Financial documentation submitted by sub-recipients on a reimbursement basis received detailed analysis by staff for CDBG eligibility compliance and cost reasonableness.

• The mid-year and annual monitoring of sub-recipients was a high priority of the Housing Department and resulted in pinpointing deficiencies of certain sub-recipients monitored and taking appropriate follow-up actions to address these deficiencies.

• Housing Rehabilitation Program production, including CDBG and non-CDBG funded projects—was maintained at a consistently high level, although program staffing has been gradually reduced by 30% since 2002. The overall administrative/ project delivery cost was deemed satisfactory, given the large size of the City’s rehabilitation program. The electronic tracking of project-specific and work-timeline data was an effective tool for managing the program.

We discussed the results of our review, as well as offered several recommendations during the monitoring exit conference held on September 14th, 2007, with you, Ms. Karen Wing, Housing Department Division Manager, and Ms. Sandra Murillo, Housing Department Policy and Planning Administrator. No findings or concerns are contained in our attached monitoring report.

If you have any questions, please contact Rafael Cediillos, at (415) 489-6585.

Sincerely,

Original signed by

Steven B. Sachs
Director, Community Planning and Development Division

Enclosure

cc: Debra Figone
City Manager
Karen Wing
Division Manager, Housing Department (HD)
Sandra Murillo
Policy and Planning Administrator, HD
Don Ludwig
Housing Rehabilitation Program Supervisor, HD
Addendum

City of San Jose -- 2007 On-site Monitoring
Community Development Block Grant (CDBG) Program
August 28-30 & September 5, 2007

Compliance with Eligibility and National Objectives Requirements

Based on project file documentation, we determined that all of the public services and neighborhood improvement activities and housing rehabilitation projects selected for our review were eligible under the CDBG program as per 24 CFR 570.201 and 202 of the program regulations, respectively. In addition, the City complied with the 15% public service cap for the 2005-06 and 2006-07 program years reviewed.

The activities in the City’s CDBG program complied with the applicable national objectives, in order to meet the low and moderate-income benefit requirements. Additionally, The City expended the majority of CDBG Program funds and program income toward activities benefiting low-and moderate-income persons, exceeding the minimum 70% threshold for the periods designated in respective annual action plans.

Sub-recipient Administration

Policies and Procedures Manuals

The City employs two very comprehensive and detailed documents to manage community (public) services and community development improvement sub-recipients and their CDBG funded projects, namely, the Policy and Procedures Manual and the Construction Policy and Procedures Manual. These documents extensively cover all contractual, financial and record-keeping obligations and procedures applicable to sub-recipients, the City’s progress-tracking and monitoring process and the implementation of construction contracts for applicable projects. HUD’s financial management/audit requirements, including those cited in OMB circulars are incorporated into the manuals.

The measurement of program effectiveness, in terms of benefits and positive changes received by low and moderate income persons and households in the community was also an important component of the City’s administration of its sub-recipients and the CDBG Program overall.

Files Review

We reviewed the files of 10 sub-recipients implementing public service, minor home improvement and neighborhood improvement activities. File documentation was well-organized and complete and included detailed sub-recipient agreements, program performance management goals, quantified objectives and timetables, approved budgets and reimbursement of funds requests, as well as quarterly reports which tracked the attainment of proposed actions and
beneficiary data by quarter and cumulatively. The City utilized a two-year budget allocation process through Program Year (PY) 2006-07, which required satisfactory performance evaluations of sub-recipients as a condition of second year funding. However, beginning with PY 2007-08, the City has opted to use a one-year budget allocation process, which will permit a more effective assessment of sub-recipient performance.

Sub-recipient Monitoring

All sub-recipients received a mid-year and end-of-the-year on-site monitoring review of CDBG funded projects, which was reflected in the files we reviewed. Monitoring documentation included questionnaires regarding progress and correspondence describing the monitoring results and required actions, as needed.

Economic and Social Opportunities, Inc. (ESO)

The City’s records indicated that one of the sub-recipients selected for our file review, namely, Economic and Social Opportunities, Inc. (ESO) was determined to lack adequate financial support information during the City’s annual on-site monitoring of the agency held during May 2005. Consequently, a Corrective Action Plan was drafted, approved and sent to the agency in November 2005. In addition to addressing issues uncovered as a result of the site visit, the Corrective Action Plan required ESO to address findings in its 2003-04 financial audit, which stated that ESO’s financial condition “could affect the Agency’s ability to continue operations.” During two February 2006 site visits, ESO did not provide requested invoices and documentation on allocation of costs to the CDBG program.

A review of the agency’s 2004-05 audited financial statement identified five findings. The findings were: 1) Accounting records were inadequate, 2) Fixed assets list was not updated, 3) Salaries and wages were not supported by personnel activity reports, 4) Cost allocation plan was not being followed, and 5) Changes to wage and salary contract allocations lacked approval documentation. ESO adequately responded to three of the five findings.

CDBG staff conducted a follow-up site visit in May 2006 and determined that financial documentation was inadequate to comply with a March 15, 2006 funding condition for PY 2006-07. This condition required ESO to provide complete and accurate documentation for fiscal expenses during 2005-06. ESO partially complied with the documentation requested and funding was released based on verification of supporting documentation by City staff. For Program Year 2006-07, staff continued to scrutinize documentation and funded only verified staff costs and fully documented non-personal costs. Ninety-two thousand dollars of fully documented costs were reimbursed. Of the remaining $468,000 balance, $115,000 in reimbursement requests were withheld due to lack of documentation. The remaining $353,000 was recaptured after formal announcement that ESO filed bankruptcy earlier this year.

In order to determine if ESO’s work was performed at specific properties, the City relied on inspection repair checklist assessments that were signed by a resident of the property when the work was completed. During FY 2006/07, several random calls were made to clients who indicated that the repairs they applied for were completed or underway. According to
management staff, the City relied on invoices, proof of payment, journal entries, timesheets, payroll registers and accounting records showing allocation of costs to CDBG—to determine if actual costs paid by CDBG were eligible and reasonable.

Based on our review of ESO file documentation and interviews with management and project management staff, we determined that the Housing Department and previously the Parks Recreation and Neighborhood Services Department—carried out timely monitoring of ESO and appropriate measured actions to address the organizational and programmatic deficiencies found, in order to improve ESO’s effectiveness and protect CDBG funds.

However, given that the City of San Jose, County of Santa Clara and the cities of Mountain View, Palo Alto and Milpitas, have separately provided CDBG funding to ESO in prior years—HUD has requested all of these communities to jointly re-evaluate whether costs incurred by ESO and paid with CDBG funds were eligible and properly documented for the 2005-06 and 2006-07 CDBG program years. HUD is particularly concerned with potential multiple-counting of same costs and the true per-unit production cost. The City and other CDBG grantees are currently researching this information in response to a HUD request. Any disallowed costs and/or unsubstantiated costs found pertaining to ESO’s CDBG funded activities during these two program years (and prior years, if requested by HUD), may require to be repaid to the CDBG Program by the respective grantee.

**Housing Rehabilitation Program**

**Production Levels and Project Delivery Cost Ratio**

The City’s Housing Rehabilitation Program generally provides CDBG funds for the moderate rehabilitation of single-family homes occupied by low and moderate-income households. The program is also a principal tool in City-coordinated neighborhood revitalization and Strong Neighborhood Initiative efforts and an adjunct to code enforcement activities.

Our monitoring of this major CDBG funded program consisted of reviewing the files of 12 completed rehabilitation projects randomly selected from client rosters and Rehabilitation Policies, Procedures and Standards. File documentation was complete and consistent and covered the application, initial inspections, lead-based paint testing and abatement in accordance with HUD requirements for the level of project funding, loan approval and execution, contractor bid review, construction management and financial tracking.

We performed several tests to measure production and cost efficiency and determined that the City’s housing rehabilitation program was very productive. Production for PYs 2005-06 and 2006-07, was computed at 21 and 22 units completed per staff Full Time Equivalent (FTE), which was derived as a result of 305 units/14.5 FTEs and 291 units/13.5 FTEs, respectively. This rate is at the upper quartile for
a program which primarily funds loans of approx. $15,000/unit. Although the City’s housing rehabilitation staff has been gradually reduced by more than 30% since PY 2002, the rehabilitation workload has remained significantly high.

The Administrative/Project Delivery Cost Ratio, which compares total rehabilitation program administrative and operational costs to total funding (CDBG and non-CDBG) for completed projects was computed at 0.36 and 0.37 for PYs 2005-06 and 2006-07, respectively. Optimally, this ratio should fall within the 0.20 and 0.35 range. However, it has been our experience that grantees with large rehabilitation programs tend to reflect APDC ratios in the low or mid-30’s. This is still deemed satisfactory because their high level of production is spread over a large number of projects, which results in increased staff time per project and the project delivery cost. This was indicative of San Jose’s rehabilitation program performance during the period reviewed.

During the past Program Year the City requested and received from HUD, technical assistance to help it create a Housing Rehabilitation Revolving Loan Fund, which is planned for the 2007-08 Program year. The RLF will dedicate CDBG program income received from CDBG loan repayments solely to housing rehabilitation activities.

Anti-Graffiti Program

The City’s Anti-Graffiti Program supplements various City neighborhood improvement efforts throughout its lower income Strong Neighborhood Initiatives target areas, as a means of preventing deterioration of these areas. The AGP is carried out by the City’s Parks, Recreation and Neighborhood Services (PRNS) Department, as a City sub-recipient agency. This activity is eligible as a rehabilitation activity and requires that the owners of each serviced property to be low and moderate-income or in the case of a rental property, that at least 51% of the residents be low and moderate-income.

The Housing Department monitored the AGP in May 2007, and determined that the majority of approximately 380 cases were properly documented, although a small percentage of the subject properties had incomplete intake documentation during PY 2006-07. Housing Department staff reviewed CDBG program requirements in-detail with PRNS management and project staff. Consequently, the client intake package and procedures were updated and utilized by PRNS during the remainder of PY 2006-07.

Interim Assistance/ Neighborhood Clean-up and Improvement Activities

San Jose Conservation Corps – Community Projects

The San Jose Conservation Corps (SJCC), a non-profit organization and CDBG sub-recipient, utilizes CDBG funds to carryout “interim assistance/one-time” clean-up and improvement activities in specific neighborhoods, which comprise the larger Strong Neighborhood Initiatives (SNI) target areas. File documentation for PYs 2005-06 and 2006-07 identified the broad SNI target areas as receiving the activities. It was only apparent from the narrative descriptions of completion reports provided by SJCC to the City (which contained
street-by-street boundaries), that specific sub-neighborhood areas within each SNI target area were serviced on a "one-time" basis.

Effective for PY 2007-08, the Housing Department is now requiring San Jose Conservation Corps to identify the sub-neighborhood service areas receiving interim assistance/one-time clean-up and improvement activities by Census block groups within each Strong Neighborhood Improvement target area. SJCC will also be required to more closely coordinate its activities with the City's SNI Team Manager. This will better help to facilitate self-sufficiency efforts by neighborhood organizations and residents and prevent further deterioration of the area immediately after the SJCC activities are completed in each sub-neighborhood service area.

**Expenditure of Funds Timeliness**

By April 30th of each year, i.e., 60-days prior to the end of the program year--a CDBG grantee is required to maintain a balance of unexpended CDBG funds that is not greater than 1.5 times its annual CDBG entitlement grant. The City has been able to meet this threshold consistently. This program performance is commendable given the size of the City’s CDBG Program annual allocation from HUD (approx. $12 million dollars), the high number and varied types of projects and activities, plus the fact that it must first expend over $1.5 million dollars in program income, mainly generated by rehabilitation loan repayments.