



2022 Fiscal Year Quarter 2: Procurement, Contract and Expenditure Review

Deloitte & Touche LLP August 10, 2022

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August 10, 2022
Honorable Jane Hughson
Mayor
City of San Marcos
630 E Hopkins
San Marcos, TX 78666

Dear Mayor Hughson:

We are pleased to provide the attached Internal Audit Report with respect to internal audit services performed for procurement and finance activities related to the Housing and Urban Development (HUD) Community Development Block Grant - Disaster Recovery (CDBG-DR) funding the City of San Marcos, Texas (the City) received as a result of the May 2015 (DR-4223) and October 2015 (DR-4245) floods. This work was performed based on the terms outlined in the engagement letter dated April 10, 2017. The areas covered during the internal audit were jointly identified with the City according to a risk-based internal audit plan and is outlined within this report.

Our services were performed in accordance with the Statement on Standards for Consulting Services issued by the American Institute of Certified Public Accountants (AICPA). However, our services did not constitute an engagement to provide audit, compilation, review, or attestation services as described in the pronouncements on professional standards issued by the AICPA, and, therefore, we will not express an opinion or other form of assurance with respect to our services.

In addition, our services did not constitute an examination or compilation of prospective financial information in accordance with standards established by the AICPA. We did not provide any assurance regarding the outcome of any future audit or regulatory examination or other regulatory action; nor did we provide any legal advice regarding our services; the responsibility for all regulatory and legal issues with respect to these matters resides with the City. It is further understood that the City is responsible for, among other things, identifying and ensuring compliance with laws and regulations applicable to the City's financial statement activities.

This report is intended solely for the information and use of City and is not intended to be, and should not be, used by any other party, with the exception of oversight agencies for the performance of their oversight responsibilities.

We appreciate the cooperation received from management and staff of the City during the performance of this internal audit.

Very truly yours,

Deloitte & Touché LLP

Kathie Schwerdtfeger, Partner

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Executive Summary

Background

The City has been awarded approximately \$34 million in Community Development Block Grant Disaster Recovery (CDBG-DR) grants by the U.S. Housing and Urban Development Department (HUD) as a result of the significant flooding events of May and October 2015. This funding is subject to federal compliance requirements found in 2 CFR §200 *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* and 24 CFR §570 *Community Development Block Grants*. Based on the HUD Action Plan developed by the City, the funds were allocated for the development of infrastructure and housing projects. To oversee the spending and oversight of the grant funds received, the City has developed policies and procedures to administer the CDBG-DR program. As needed, contracted professionals are engaged to provide additional technical assistance. Additionally, the City developed CDBG-DR policies and procedures, established internal controls, and implemented systems to govern the use of the HUD funds received.

In accordance with requirements set forth by HUD, The City has engaged Deloitte & Touché LLP to conduct internal audits each year of program funds and activities to evaluate compliance with national objectives, the City's HUD CDBG-DR Action plan and related amendments, federal program regulations, and City policies and procedures related to the CDBG-DR funding. Additionally, the internal audits evaluate the design and operating effectiveness of internal controls over program activities and funds and provides recommendations for enhancement, when needed.

Our Scope & Objectives

The area of focus for this internal audit included procurement, contracts, and finance activities for CDBG-DR activities occurring in the City's first quarter of Fiscal Year 2022 from January 1, 2022 through March 31, 2022.

Each area was reviewed to evaluate the following:

- The design and operating effectiveness of internal controls of the Finance and Purchasing Departments
- Compliance with Federal program and administrative regulations governing the CDBG-DR program
- Compliance with City policies and procedures governing the CDBG-DR program
- Compliance with the City's HUD Action Plan for Disaster Recovery and related amendments

Procurement and Contracting:

The assessment procedures included evaluation of the contract front-end life cycle, from request for proposal (RFP) to the establishment of a contract. The procurement process was evaluated for the services listed below and included the procurements for which an RFP was issued under these grants between January 1, 2022 through March 31, 2022. Contracts resulting from the procurement process were also reviewed in addition to procurements and/or contracts not provided in previous quarters.

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Expenditures:

The assessment procedures evaluated whether federal regulations and City policies and procedures were followed in the approval and payment of CDBG-DR related expenditures during the period of January 1, 2022 through March 31, 2022. The selected expenditures were also evaluated to determine whether they were reasonable, necessary, allowable, and properly evidenced by supporting documentation. A sample of expenditures was selected from program expenditures for the period and included infrastructure, housing, administration, and planning activities.

The testing methodology included an analysis of at least 30% of the transactions executed during the period and consisted of an evaluation of invoices, proof of payment, general ledger, the HUD Quarterly Performance Reports (QPR) and HUD Disaster Recovery Grants Reporting System (DRGR) reporting and compliance with applicable policies, procedures, and federal grant regulations.

Prior Audit Findings:

The assessment procedures utilize interviews and follow-up meetings with City staff to review the status of resolution or evidence of progress relating to any prior audit findings from prior quarterly internal audits, HUD monitoring visits, or other external audits with findings directly related to the CDBG-DR program. We also reviewed the City's progress on the corrective action plan from the previous Quarter's reports.

The City underwent a HUD monitoring visit in August of 2021. HUD's Monitoring Report was issued on November 24, 2021. No new findings or concerns were identified and all prior findings from the June 2020 visit were considered resolved. The report did provide the following recommendation regarding the City's Housing Programs, "HUD recommends a thorough assessment of all supporting documentation within each project/activity file under each program prior to closeout." This recommendation aligns with the Internal Audit Plan outlined in Deloitte's Annual Risk Assessment issued in November 2021 and will be reported on as part of the Quarter 2 Housing Program review which is underway now and will be completed in September 2022.

Approach

The internal audit activities performed included the following:

- **Step 1:** Interviewed the following key stakeholders involved in administering the CDBG-DR program to gain an understanding of program activities during the period and obtain their input related to potential risks to the program:
 - Anna Miranda - Interim Finance Assistant Director
 - Carol Griffith - Housing and Community Development Manager
 - Zindi Castillo - Grants Accounting Specialist
 - Jacquelyn Thomas - Senior Engineer
 - Jesse Garcia - Finance Grants Manager
 - Lynda Williams - Purchasing Manager

- **Step 2:** Performed the following review and testing procedures:
 - **CDBG-DR Contracts**
 - Obtained procurement and contract related documents for procurement and contract activities that occurred during the period.
 - Assessed the City of San Marcos Action Plan for Disaster Recovery and the City's Purchasing Policy to verify consistency and adherence with federal regulations and HUD policy;
 - Evaluated RFP and Contract activity since the last internal audit to determine whether they were consistent with the City's procurement policy;
 - Assessed the RFP and bid review evaluation process;
 - Evaluated contracts established for required Federal clauses;
 - Identified areas for improvement and developed recommendations for consideration.
 - **CDBG-DR Expenditures**
 - Obtained expenditure data for program expenditures that occurred during the period.
 - Selected approximately 30% of expenditures for testing from General Ledger with a focus on activities with high spend during the period;
 - Assessed purchase or approval processes related to work performed;
 - Evaluated invoices for contracts established and associated purchase orders
 - Evaluated labor, equipment, and other charges based on rates and amounts and mathematical accuracy and reasonable of invoice and/or allocation methods; and Evaluated invoice review processes.
- **Step 3:** Conducted a closing meeting and discussed the observations and recommendations with management.

Observations and Recommendations

As noted on page 4 of this report, Observations and Recommendations, including Management Response & Corrective Action Plan are presented and addressed herein.

Observation Category	Observation	Observation	Recommendations/Management Action Plans
	Condition	Criteria, Cause, Effect	Recommendation
Q2 Expenditure Review	No expenditure related observations were identified this quarter.		
Q2 Drawdown Review	<p>1D-a. In one (1) instance, both voucher creation and drawdown occurred in FY22 Q3 rather than in the quarter when the expenditure was incurred or shortly thereafter.</p> <p>It has been noted that the remaining six (6) drawdowns occurred within the same month.</p> <p>Though improvement has been made in this area, this finding has been noted in previous quarters.</p>	<p>Per 2 CFR 200.302(b)(2), Financial Management, recipients of funding are responsible for accurate, current, and complete disclosure of the financial results of each Federal award or program.</p> <p>In prior monitoring visits HUD identified the City as a slow spender of HUD CDBG-DR funds. In response, the City committed to avoid delays to spending and drawdowns.</p>	While the City's current policy encourages monthly drawdowns, it should consider amending this procedure to require City staff to draw down funds monthly or biweekly to better tie federal drawdowns to federal program expenditures occurring in the period. In not doing so, the City is covering federal program costs with City general revenue for a longer period of time than strong financial management would advise.
	<p>1CO-a. CoSM Response:</p> <p>The City is committed to improving processes to request more timely drawdowns. Key staff vacancies have been filled as of February 2022. The expectation is that drawdown of funds will occur at least monthly going forward.</p>		

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Observation Category	Observation	Observation	Recommendations/Management Action Plans
	Condition	Criteria, Cause, Effect	Recommendation
Q2 Procurement Review	No procurement related observations were identified this quarter.		
	1CO-a. CoSM Response:		
Q2 Change Orders Review	No change order related observations were identified this quarter.		

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