



**OFFICE OF THE INSPECTOR GENERAL**  
*City of Chicago*

Joseph M. Ferguson  
*Inspector General*

180 N. Michigan Avenue, Suite 2000  
Chicago, Illinois 60601  
Telephone: (773) 478-7799  
Fax: (773) 478-3949

To: Mayor Richard M. Daley  
Members of the City Council

From: Inspector General Joseph Ferguson

Re: Central Loop and Central West TIF Audit

Date: June 29, 2010

The Inspector General's Office has completed an audit of processes and procedures related to Tax Increment Financing (TIF) expenditures between January 1, 2003 and December 31, 2007 for the Central Loop and Central West TIF districts. Additionally, we reviewed TIF district porting and transfers for the years 1997 through 2007. As you know, the City of Chicago uses TIF as an economic development tool to promote private redevelopment of commercial, industrial, and residential sites throughout the City. A core purpose of TIF is to support public projects and incentivize private development in economically depressed areas which have difficulty attracting development investment. It does so through a 23-year set aside of property tax revenues above a specified base. Portions of the resulting specified future tax revenue stream may then be collateralized for major development project financing and also used for direct governmental support to broaden and deepen the area's economic and infrastructure base critical to robust and sustainable redevelopment in a community. Among other things, TIF is commonly used to finance public and private ventures such as building rehabilitation, construction of affordable housing, development of public parks, schools, infrastructure improvements, as well as job-training and day care programs.

Our purpose was to test and evaluate activities performed to ensure effective and efficient operations, compliance with policies and procedures, and to evaluate the effectiveness of controls related to the payment of expenditures using TIF funds. A copy of the audit report is attached.

In overview, the audit found that internal controls were *not* adequate to ensure effective management of the TIF expenditures we reviewed, as related to the State of Illinois TIF Act, 65 ILCS 5/11-74.4 *et seq.* ("The TIF Act"). Additionally, we conclude that TIF-related processes are not sufficiently transparent. More specifically, the audit found, among other things, that as a result of the inadequacy of certain internal controls:

- Excess and unused TIF funds from the Central Loop TIF district for Millennium Park and the Harold Washington College Rehabilitation project, totaling approximately \$1.2 million, were left

with the Public Building Commission for almost 3 years, and well beyond the expiration of the TIF.

- The Public Building Commission improperly paid to the City of Chicago Department of Cultural Affairs \$329,000 in TIF funds for the purchase of art work, in violation of the TIF Act, which expressly prohibits such expenditures from TIF funds.
- Money acquired from liquidated damages for construction projects managed by the Public Building Commission with Central Loop TIF funding, totaling \$85,000, was improperly used to fund a training program outside the Central Loop TIF district and therefore was not an authorized Central Loop TIF expenditure.
- Costs associated with an Intergovernmental Agreement that was never approved between the City of Chicago and the Chicago Park District for use of the Police Academy were incurred by the Central West TIF district. Renovation expenditures required by the Park District in anticipation of more extensive usage had the IGA been finalized were made and approved by City employees managing the Police Academy renovation. This resulted in expenditures totaling \$89,753.74 that were not duly authorized in the absence of a finalized IGA and were questionable on their own terms.
- City of Chicago employees responsible for managing the Chicago Police Academy renovation, acting in concert with private contractors, utilized deceptive billing practices to acquire certain products or services not included in the approved purchasing system to avoid subjecting the acquisitions to applicable processes and scrutiny of the Department of Procurement Services.
- Assessments totaling \$54,266.26 against contractors who failed to meet City requirements for Minority and Female Journeyworkers, Minority and Female Apprentices, Minority and Female Laborers, and Chicago Residency requirements in the performance of TIF-paid work on the Police Academy Renovation had not been collected some 2 years after the work was completed.
- Administrative policies and procedures for TIF allocation of salary and overhead costs are insufficient and in some respects non-existent.
- Decisions to move money from one TIF district to another contiguous district – so-called “porting” of funds – are not adequately documented and are made without sufficient transparency to assure adequate accountability and public scrutiny.

As noted in the auditor’s report, the management and staff of the Departments of Community Development, Finance, Procurement Services, General Services, Cultural Affairs, Office of Budget and Management, and the Public Building Commission provided full cooperation during the audit. These and other City Departments provided information and clarification regarding the use of TIF funds which have facilitated the successful completion of the audit. Prior to publication, we made our findings and recommendations available to relevant City management officials. In many respects, City management officials have acknowledged the audit findings and acted promptly to implement remedial measures responsive to specific audit findings and recommendations, including securing the recovery of substantial funds identified by the IGO

audit. In other respects, there was disagreement regarding our conclusions and recommendations respecting certain of the findings. The City's responses are included in our final report. Stated areas of disagreement should be viewed principally as reflective of a constructive dialogue across and between governmental components working toward the shared objective of providing effective, efficient services in a manner that complies with state and local law, and is transparent and accountable to the residents of the City.

cc: Chief of Staff Raymond Orozco  
City Comptroller Steven J. Lux  
Budget Director Eugene Munin  
Corporation Counsel Mara Georges  
Chief Procurement Officer Jamie Rhee  
Commissioner Judy Martinez, Department of General Services  
Commissioner Christine Raguso, Department of Community Development  
Commissioner Lois Weisberg, Department of Cultural Affairs  
Superintendent Jody P. Weis, Chicago Police Department  
Director of Intergovernmental Affairs Joan Coogan  
Executive Director Erin Lavin Carbonargi, Public Building Commission



**OFFICE OF THE INSPECTOR GENERAL**  
*City of Chicago*



***REPORT OF THE INSPECTOR GENERAL'S OFFICE:***

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***TAX INCREMENT FINANCING EXPENDITURE AUDIT - 2008***

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**TABLE OF CONTENTS**

**AUDITOR’S REPORT .....1**

**EXECUTIVE SUMMARY .....2**

**BACKGROUND.....5**

    Introduction .....5

    Creation of a TIF District.....7

    Providing TIF Assistance for Development Agreements .....8

    Providing TIF Assistance for Inter-Governmental Agreements .....9

    Providing TIF Assistance for Infrastructure Projects.....9

    TIF Funds Used to Reimburse the City for Administrative Costs .....10

    Audit Expenditure Review - Selection and Examination .....11

**SCOPE & METHODOLOGY.....13**

**OBJECTIVES.....13**

**PURPOSE .....13**

**AUDIT FINDINGS AND RECOMMENDATIONS.....15**

    Finding 08-01: Insufficient Monitoring and Reconciliation of Funds and Expenditures Resulted in \$1,202,496.89 in Unused Central Loop TIF Funds Remaining at the PBC for Nearly Three Years ..... 15

        Recommendation 08-01: .....15

        City Response: .....16

    Finding 08-02: The PBC Improperly Paid to the Department of Cultural Affairs \$329,000 in Central Loop TIF Funds for the Purchase of Public Art, a Non-Eligible Expense, in Violation of the TIF Act .....17

        Recommendation 08-02: .....18

        City Response: .....18

    Finding 08-03: \$54,266.26 in Contractor Assessed Liquidated Damages Due the Central West TIF Have Not Been Collected..... 19

        Recommendation 08-03: .....20

        City Response: .....20

        IGO Response to City Response: .....21

    Finding 08-04: Employees of DGS Engaged in Deceptive Billing Practices in Conjunction with Old Veterans Construction and Paul Borg Construction in Transactions Involving the Use of TIF Funds.....22

        Recommendation 08-04: .....23

        City Response: .....24

        IGO Response to City Response: .....24

    Finding 08-05: \$89,753.74 of Central West TIF Money Was Spent on Questionable Expenditures .....25

        Recommendation 08-05: .....26

        City Response: .....26

    Finding 08-06: Liquidated Damages Were Used in Violation of the TIF Act to Fund Ineligible Training Program Expenditures of almost \$85,000 to a Program Outside of the TIF District .....27

        Recommendation 08-06: .....28

        City Response: .....28

        IGO Response to City Response: .....29

    Finding 08-07: Fitness Equipment Purchased for the Police Academy Workout Room Resulted in \$39,773.99 of Wasted TIF Funds and Two 32 Inch Flat Screen TV’s Valued at approximately \$577 each were Stolen by an Employee of the Ordering Contractor .....30

        Recommendation 08-07: .....32

        City Response: .....32

        IGO Response to City Response: .....33

Finding 08-08: Costly Material Selections for the Police Academy Wasted \$18,297 .....34  
 Recommendation 08-08: .....34  
 City Response: .....35  
 IGO Response to City’s Response: .....35  
 Finding 08-09: Poor Controls Allowed Expenditures to be Paid that were Non-Eligible or Unauthorized  
 Uses of TIF Funds .....36  
 Recommendation 08-09: .....37  
 City Response: .....37  
 Finding 08-10: Administrative Policies and Procedures for TIF Allocation of Salary and Overhead Costs  
 are Non-Existent .....38  
 Recommendation 08-10: .....42  
 City Response: .....43  
 Finding 08-11: WBE Credit Related to Vendor Subcontracts was Miscalculated and Based on  
 Misrepresentation .....44  
 Recommendation 08-11: .....45  
 City Response: .....45  
 Finding 08-12: Expenditures Submitted to the City of Chicago by the PBC for Reimbursement are Not  
 being Reviewed for Compliance with the TIF Act .....46  
 Recommendation 08-12: .....47  
 City Response: .....48  
 IGO Response to City Response: .....48  
 Finding 08-13: Calculations Used for Determining Income Eligibility to Purchase TIF Subsidized  
 Housing were Inappropriate.....49  
 Recommendation 08-13: .....50  
 City Response: .....50  
 Finding 08-14: The Decision to Port Money is Determined by Non-Elected City Employees called the  
 “TIF Task Force” with no Disclosure to Taxpayers or the City Council until Annual Reports are Filed.....51  
 Recommendation 08-14: .....52  
 City Response: .....52  
 IGO Response to City Response: .....53  
 Finding 08-15: Material Ordered Directly by DGS In-House Trades was not Properly Verified as  
 Received Resulting in the Potential for Theft.....54  
 Recommendation 08-15: .....54  
 City Response: .....55

## **AUDITOR'S REPORT**

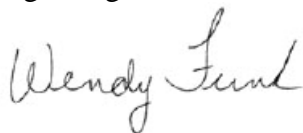
The mission of the Inspector General's Office (IGO) is to root out corruption, waste and mismanagement, while promoting effectiveness and efficiency in the City of Chicago. The IGO Audit Unit conducts independent and professional audits, reviews, and evaluations of the operations of City departments, programs, functions, and those doing business with the City. These engagements focus on the integrity, accountability, economy, efficiency and effectiveness of each audit subject.

We completed an audit of processes and procedures related to Tax Increment Financing (TIF) expenditures between January 1, 2003 and December 31, 2007 for the Central Loop and Central West TIF districts. Additionally we reviewed all TIF district porting and transfers for the years 1997 through 2007. The fieldwork was performed between August 2008 and October 2009. The authority to perform such an audit is established in the *City of Chicago Municipal Code §2-56-030* which states the Inspector General's Office has the power and duty to promote economy, efficiency, effectiveness and integrity in the administration of programs and operations, as well as identify any inefficiencies, waste and potential for misconduct.

Our purpose was to test and evaluate activities performed to ensure effective and efficient operations and compliance with policies and procedures, and to evaluate the effectiveness of controls related to the payment of expenditures using TIF funds. We conducted this audit in accordance with generally accepted Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Based upon the results of our audit, we determined internal controls are not adequate to ensure effective management of TIF expenditures as related to the State of Illinois TIF Act, 65 ILCS 5/11-74.4 et seq. first adopted in 1977 and amended from time to time.

We would like to thank the management and staff of the Departments of Community Development, Finance, Procurement Services, General Services, Cultural Affairs, Office of Budget and Management, and the Public Building Commission for their cooperation during the audit. Their assistance contributed significantly to the successful completion of the audit. In addition, we would like to thank all departments that researched and provided clarification regarding the use of TIF funds.



Wendy Funk  
Chief Auditor

## EXECUTIVE SUMMARY

We completed an audit of processes and procedures related to Tax Increment Financing (TIF) expenditures between January 1, 2003 and December 31, 2007 for the Central Loop and Central West TIF districts. Additionally we reviewed TIF district porting and transfers for the years 1997 through 2007. Our purpose was to test and evaluate activities performed to ensure effective and efficient operations and compliance with policies and procedures, and to evaluate the effectiveness of controls related to the payment of expenditures using TIF funds.

Based upon the results of our audit, we determined internal controls were not adequate to ensure effective management of TIF expenditures we reviewed, as related to the State of Illinois TIF Act, 65 ILCS 5/11-74.4 et seq. first adopted in 1977 and amended from time to time. Additionally we believe that TIF-related activities are not sufficiently transparent.

This summary highlights the key findings which are described in detail within the Audit Findings and Recommendations section beginning on Page 15.

*CENTRAL LOOP TIF FUNDS TOTALING \$1,202,496.89 REMAINED WITH  
THE PUBLIC BUILDING COMMISSION (PBC) FOR ALMOST 3 YEARS.*

Excess TIF funds from the Central Loop TIF district for Millennium Park and the Harold Washington College Rehabilitation projects remained unused with the Public Building Commission (“PBC”) for almost 3 years. It was not until the IGO auditors discovered the excess funds thru this audit that action was taken to secure the return of the money. However, since the Central Loop TIF district had already expired when the excess funding was discovered by the IGO, the money had to be returned to the County, thus reducing the amount available by the City for use within the Central Loop TIF district. The IGO recommends, among other things, that the City perform quarterly reviews and reconciliations of TIF expenditures and cash on hand.

*THE PUBLIC BUILDING COMMISSION (PBC) PAID THE DEPARTMENT OF  
CULTURAL AFFAIRS (DCA) \$329,000 FOR ART WORK IN VIOLATION OF  
THE TIF ACT.*

The City of Chicago established the Public Art Program which budgets money from public building construction for the purpose of establishing a method to fund art work included in buildings that have public access. The TIF Act does not allow for this type expenditure. In violation of the TIF Act, the DCA invoiced the PBC for \$329,000 for art work.

Our audit discovered the improper payment of TIF funds to the DCA and recommended that the money be returned to the City and consequently to the County since the Central Loop TIF district from which the funds originally were remitted had expired.



*MONEY ACQUIRED FROM LIQUIDATED DAMAGES FOR CONSTRUCTION PROJECTS MANAGED BY THE PBC WITH CENTRAL LOOP TIF FUNDING TOTALING ALMOST \$85,000 WAS USED TO FUND AN INELIGIBLE TRAINING PROGRAM.*

The TIF Act 65 ILCS 5/11-74.4-3(q)(5) specifies that “Costs of job training and retraining projects, including the cost of ‘welfare to work’ programs implemented by business located within the redevelopment project area” are TIF eligible. The Skill Builders Program for which the above money was used is located at 5410 South State Street clearly outside of the Central Loop TIF area and therefore was not an eligible TIF expenditure.

*CITY OF CHICAGO EMPLOYEES AND CONSTRUCTION CONTRACTORS ENGAGED IN DECEPTIVE BILLING PRACTICES DURING THE RENOVATION OF THE CHICAGO POLICE ACADEMY.*

Billing submitted by contractors for the acquisition of products and services used in the renovation of the Police Academy utilizing Central West TIF district funds did not always match actual products or services received. Employees responsible for managing the Police Academy renovation acted in concert with contractors to manipulate the billing to acquire products or services not included in the approved purchasing system in order to avoid using the Department of Procurement Services.

*QUESTIONABLE TIF EXPENDITURES IN THE AMOUNT OF \$89,753.74 WERE FOUND IN THE RENOVATION OF THE CHICAGO POLICE ACADEMY.*

Costs associated with an Intergovernmental Agreement (IGA) *that was never approved* between the City of Chicago and the Chicago Park District for use of the Police Academy were incurred by the Central West TIF district. Renovation expenditures required by the Chicago Park District in anticipation of more extensive usage had the IGA been finalized were made and approved by City employees managing the Police Academy renovation, resulting in expenditures totaling \$89,753.74 that were neither duly authorized in the absence of a finalized IGA and were questionable on their own terms.

*CONTRACTOR ASSESSED LIQUIDATED DAMAGES TOTALING \$54,266.26 DUE THE CENTRAL WEST TIF DISTRICT HAVE NOT BEEN COLLECTED.*

Assessments totaling \$54,266.26 against contractors who failed to meet City requirements for Minority Journeyworkers, Female Journeyworkers, Minority Apprentice and Female Apprentice, Minority Laborer, Female Laborer, and Chicago Residency requirements in the performance of TIF-paid work on the Police Academy Renovation had not been collected some 2 years after the work was completed. Additionally, the City has not retained the appropriate holdback required to offset these amounts from contractor payments thereby jeopardizing the return of this money to the TIF district.

*PORTING OF TIF FUNDS BETWEEN CONTIGUOUS TIF DISTRICTS IS DETERMINED BY A SMALL GROUP OF CITY EMPLOYEES WITHOUT ADEQUATE TRANSPARENCY.*

Decisions to move money from one TIF district to another are made without documentation and without public scrutiny. City Residents who contribute real estate tax dollars to the TIF district from which money is being removed are being deprived of full and transparent disclosure of and access to the factual bases and rationale behind the diversion of their property tax dollars to another TIF district. TIF districts are established for the benefit of the residents and businesses within that district. The comparative lack of transparency in the porting process perpetuates the notion of a secret process subject to undue influence from self-interested parties looking to exploit the TIF for personal gain.

In addition to the findings highlighted in this summary the audit report includes detailed information relating to other findings of waste, abuse, non-compliance and insufficient internal controls that contribute to our audit conclusion that controls are not sufficient to ensure effective management of TIF expenditures. The audit report further includes recommendations for redressing the procedural shortcomings, the City's responses to our findings and recommendations, and in some instances, our observations regarding the City's response.

**BACKGROUND**

This section describes the Tax Increment Financing Program and its administration by the City of Chicago.

**I. Introduction**

The City of Chicago uses TIF as an economic development tool to promote private redevelopment of commercial, industrial, and residential sites throughout the City. Since the State of Illinois TIF legislation, 65 ILCS 5/11-74.4 et seq. was first adopted in 1977, more than 150 TIF Districts have been designated within the City of Chicago.

Generally, TIF is used to finance public and private ventures such as building rehabilitation, construction of affordable housing, development of public parks, schools, infrastructure improvements, as well as job-training and day care programs.

One of the purposes of TIF is to provide governmental incentives to private developers to stimulate investment in areas which have difficulty attracting development.

The basic concept behind TIF is that a portion of future property taxes are committed to supporting financial incentives for the development of areas that otherwise would not be developed in the absence of governmental assistance. For example, an area that is too costly to develop because of depressed revenue prospects remains under-utilized or vacant. Under-utilization in turn results in depressed property values. Depressed property values are a drag on property tax revenues. In concept, TIF incentivizes the generation of new revenue sources by developers that invest in an area, which improves property values and results in increased property tax revenues that are then used to recoup the costs of development incentives incurred by the City at the front end.

In order for the City to offer TIF assistance to a developer, the location of proposed projects must be within the legislatively defined boundaries of an existing TIF redevelopment area or the City must create a TIF redevelopment area or district based on certain criteria required by State statute, as discussed later. The establishment of a TIF district is a technical process which takes approximately six months to accomplish. It is subject to the approval of the City Council of Chicago. Once the district is established, the City can pay certain eligible redevelopment costs, which are outlined in the State statute 65 ILCS 5/11-74.4-3 (q) sections (§) listed as follows:

- § 1                    Cost of studies and professional services
- § 1.5                Administrative cost with limitations
- § 1.6                Marketing costs
- § 2                    Property assembly, demolition & site preparation costs
- § 3                    Private & public building rehabilitation and public building replacement costs
- § 4                    Public works construction and improvement costs; municipal public building limitations

- § 5 Job training, retraining and welfare to work costs implemented by businesses in the TIF District
- § 6 Financing costs
- § 7 Taxing district’s capital costs resulting from redevelopment
- § 7.5 TIF assisted housing school district increased costs
- § 7.7 Public library increased costs due to assisted housing units (on or after 1/1/2005)
- § 8 Relocation costs
- § 9 Payments in lieu of taxes
- §10 Job training, retaining, vocational and career education, with certain limitations
- §11 Interest cost incurred by a redeveloper related to the construction, renovation or rehabilitation of a redevelopment project with certain requirements.
- §11.5 Day care costs, with certain requirements
- §12 Limitation on new privately-owned building construction costs
- §13 Limitation regarding attraction of retailers currently located in adjacent communities
- §14 Exclusion on use of TIF funds for demolition, removal, or substantial modification of an historic resource (effective 08/2008)

Only redevelopment costs incurred by a developer on TIF-reimbursable expenditures after the district is established are eligible for TIF-financing. The costs are repaid from incremental property taxes captured in the TIF district over 23 years. The annual increase in property taxes generated within the TIF district over the base amount of property taxes in the year the TIF district was established can be used for eligible project costs as defined in the Redevelopment Agreement (RDA).

A tax increment is the difference in tax revenues collected between a baseline of adjusted tax rates on equalized assessed property valuations immediately prior to the creation of the TIF district and the amount collected after the TIF district is established. Any increase above the initial equalized assessed valuation is multiplied, on an annual basis, by the aggregate tax rate resulting from the levy of real property taxes by all units of local government having taxing power over the real property. The product of this calculation is the amount of incremental property tax revenues generated within the TIF district. The legal set-aside of tax revenues above base over a 23 year span allows the City, in the context of a TIF district, to collateralize the resulting future revenue stream to support various forms of near-term financing for long-term development projects within the TIF district.

Tax increment revenues are generated by allowing the City to capture all property tax revenues that exceed property tax revenues generated by the base equalized assessed valuation of the area before being designated for redevelopment. Property taxes are generally paid to eight different taxing districts of which the City is one. When a TIF district is created, instead of each of the taxing districts receiving their portion of the incremental property taxes, the incremental property tax revenue is deposited into special tax allocation funds specific to the individual TIF district controlled by the City from which redevelopment project costs can be paid. Under tax increment

financing, all overlaying taxing districts continue to receive real estate tax revenue only on the base calculated on the initial pre-TIF equalized assessed valuation.

## **II. Creation of a TIF District**

For an area to be designated as a TIF district, the City must demonstrate that the prospective district qualifies as a “blighted area” or as a “conservation area” within the definitions of the TIF Act (definitions effective on or after 11/1/1999 per Public Act 91-478)<sup>1</sup>. A “blighted area” may be either improved or vacant. If the area is improved, five or more of the following factors must be present and reasonably distributed throughout the improved part of the redevelopment project area: dilapidation, obsolescence, deterioration, presence of structures below minimum code standards, illegal use of individual structures, excessive vacancies, lack of ventilation, light, or sanitary facilities, inadequate utilities, excessive land coverage and overcrowding of structures and community facilities, deleterious land-use or lay out, environmental clean-up, lack of community planning, or the total EAV of the proposed redevelopment project area has declined or not increased at an acceptable rate in three of the last five calendar years.

If the area is vacant, the City must find that its growth is impaired by a combination of two or more of the following factors: obsolete platting, diversity of ownership is insufficient, tax and special assessment delinquencies, deterioration of structures or site improvements on adjacent land, the area has incurred Illinois Environmental Protection Agency (“IEPA”) or the United States Environmental Protection Agency (“USEPA”) remediation costs or will require environmental remediation, or the total Equalized Assessed Valuation (“EAV”) of the proposed redevelopment project area has declined or not increased at an acceptable rate in three of the last five calendar years. Additionally if vacant, one or more of the following conditions must exist: that the area consists of one or more unused quarries, mines, strip mine ponds, rail yards, rail tracks, or railroad rights-of-way; or the area is subject to chronic flooding, consists of an unused or illegal disposal site, and prior to 11/1/1999 the area is not less than 50 nor more than 100 acres and 75% of which is vacant, or the area qualified as a blighted improved area prior to becoming vacant.

A “conservation area” is an improved area in which 50% or more of the structures in the area have an age of 35 years or more and three or more of the following factors are present: dilapidation, obsolescence, deterioration, structures below minimum code standards, illegal use of individual structures, excessive vacancies, lack of ventilation, light or sanitary facilities, inadequate utilities, excessive land coverage and overcrowding of structures and community facilities, deleterious land use or lay out, lack of community planning, incurred costs for environmental clean-up or for a study that indicated that such clean-up is necessary, a decline in the equalized assessed valuation for three of the last five calendar years, or an increase at an annual rate that is less than the Consumer Price Index (“CPI”) for all Urban Consumers published by the US Department of Labor.

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<sup>1</sup> Prior to amendment by P.A. 91-478, the definitions of “blighted” and “conservation” areas differed slightly from current definitions, but it is not significant for purposes of background discussion in this report.

To demonstrate that the area meets these criteria, an eligibility study is conducted. At the same time, a redevelopment project and plan is created, which sets forth the City's plans for the proposed TIF district.

Eligibility studies and redevelopment project and plans are generally prepared by consultants hired by the developers and reviewed and accepted by the City, or if there is not a potential developer at the time of designation, the City hires the consultants who then prepare the plan under direction from the Department of Community Development (DCD).

Once the eligibility study and redevelopment project and plan are completed, they are presented jointly at a meeting of the Community Development Commission (CDC). The CDC is an advisory commission, whose members are appointed by the Mayor, established by the City Council in 1992 to advise the Council on development matters. Fourteen days after the TIF proposal is made to the CDC, the Joint Review Board reviews and votes on the proposal. The Joint Review Board consists of a representative selected by each taxing district having taxing power over the proposed TIF area, and a member of the public. Once the eligibility study and redevelopment project and plan are presented, the CDC orders a public hearing. The date for the public hearing is usually held two months after the initial presentation of the TIF proposal at another CDC meeting. After the public hearing, the CDC votes on the TIF proposal. If approved by the CDC, the ordinances required for the designation of the TIF district are introduced to City Council, referred to the City Council's Committee on Finance, at which time public comment is accepted, and then reconsidered by the full City Council.<sup>2</sup> The TIF designation process from start to finish takes six to twelve months, depending on whether or not a housing impact study or public meeting is needed.

### **III. Providing TIF Assistance for Development Agreements**

The Department of Community Development ("DCD") was formed on January 1, 2009, through the merger of the former departments of Planning and Development (DPD), Housing (DOH) and Mayor's Office of Workforce Development (MOWD). One of DCD's responsibilities is administration for TIF.

Each of the City TIF districts was established with unique redevelopment goals based on a redevelopment plan that addresses the broad needs of the area. Some districts are established to encourage industrial redevelopment while others promote commercial and residential redevelopment. Because there is such diversity in the planning objectives and development goals, no single criterion has been established by DCD to award TIF assistance. Each request is considered on a case-by-case basis.

To apply for TIF assistance, the developer (or designated consultant) must compile all forms required for the application process and submit them to DCD. This is the first step in the approval process and one of the administrative responsibilities of DCD.

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<sup>2</sup> Additional public hearings are required if 75 or more residential units are in the TIF, or 10 or more occupied residential units will be removed as a result of the TIF. The City must have an additional public hearing on the housing impact of the plan per subsection (a) of Section 11-74.4-5 of the TIF Act.

DCD staff work with potential developers to discuss the parameters, goals, and needs of the proposed project. Projects that seek TIF assistance are required to schedule a Pre-Qualification meeting so that the fundamentals of the project can be presented to DCD staff and so that the developer can be made aware of the type of information necessary to be submitted with a TIF application.

Once DCD has determined that the project meets the criteria required to be considered for TIF assistance DCD will work with developers to advance eligible requests to the CDC for its recommendation. TIF assistance money can be provided only after the City Council grants authority for the City and developer to enter into a redevelopment agreement.

DCD is also responsible for the pre-disbursement review of developer reimbursed TIF expenditures. As part of the redevelopment agreement the amount of TIF funding is approved by the City Council and incorporated into the agreement. DCD must review all expenditures to verify that they are allowable under the TIF Act. Once DCD has approved the expenditure as allowable it can be reimbursed. In almost all cases TIF money is provided to reimburse the developer for costs already incurred.

#### **IV. Providing TIF Assistance for Inter-Governmental Agreements**

TIF assistance is also provided for projects involving City of Chicago sister agencies such as the Chicago Transit Authority (CTA), Chicago Public Schools (CPS), Chicago Housing Authority (CHA), and the Chicago Park District whose leaders are appointed by the Mayor. Staff at DCD meets with representatives from the requesting government agencies to discuss the project merits and goals in conjunction with the TIF district plan. If the project meets the required criteria the project is reviewed by the "TIF Task Force" chaired by the Office of Budget and Management (OBM) and made up of DCD management together with City department heads participating in the project.

If the Task Force determines the project has merit consistent with the purposes and parameters of the TIF Redevelopment Plan an IGA is drafted for review by the City and by the government agency requesting TIF funds. The IGA is then reviewed and if approved by the full City Council an ordinance is passed indicating the amount of TIF funding authorized.

#### **V. Providing TIF Assistance for Infrastructure Projects**

Other types of projects funded from TIF district revenues are infrastructure projects, also considered capital spending projects. Some examples of these projects are street resurfacing, bridge and viaduct repairs, new street lighting, new sidewalks and alleys, and projects such as the riverwalk expansion, and building renovations like the Chicago Police Academy to name a few.

The infrastructure project is often identified by DCD, other City departments such as Chicago Department of Transportation (CDOT), or an alderman. Once the project has been identified, the City department responsible for the construction and/or management of the project will develop cost estimates that will be reviewed by DCD and OBM. If the funding source is determined by DCD and OBM to be from TIF revenue then the TIF Task Force headed by OBM and made up

of DCD management, and City department heads responsible for the project, reviews the cost estimates and approves the budget.

The budgeted cost approved by the TIF Task Force is then set up by the Department of Finance (DOF) under a new funding authorization allowing the City department charged with the infrastructure project management to draw down the required funds to complete the project. Once the project has been approved and the funds authorized DCD is no longer involved in the TIF expenditure review. The City department charged with the infrastructure project management is now responsible for making sure the expenditures from TIF funds are allowed under the TIF Act.

The City may at times use non-TIF funding sources for infrastructure projects. Street repairs are an example of a capital project that may be initially paid from capital project bonds and later reimbursed from TIF funds. The DOF and OBM together with DCD review available TIF district funds to determine if the projects can be reimbursed. If it is determined that the funds are available, the money is transferred from the TIF district fund to the City Corporate Fund (a general revenue fund) where it can be used for any reason, unrestricted by TIF Act expenditure requirements.

In addition to transfers, the City may also employ porting to move TIF funds from one TIF district to another. The TIF Act 65 ILCS 5/11-74.4-4 defines porting as follows:

“A municipality may:... (q) Utilize revenues, other than State sales tax increment revenues, received under this Act from one redevelopment project area for eligible costs in another redevelopment project area that is:

- (i) contiguous to the redevelopment project area from which the revenues are received;
- (ii) separated only by a public right of way from the redevelopment project area from which the revenues are received; or
- (iii) separated only by forest preserve property from the redevelopment project area from which the revenues are received if the closest boundaries of the redevelopment project areas that are separated by the forest preserve property are less than one mile apart.”

Which, simply put, is the movement of TIF money from one TIF district to another TIF district that is contiguous, separated by a public right of way, or separated by forest preserve property.

The decision to port funds is made by DCD management, sometimes in conjunction with input from the DOF and OBM.

## **VI. TIF Funds Used to Reimburse the City for Administrative Costs**

TIF funds are used to reimburse the City for administrative costs associated with employees whose function is directly related to TIF activity. In addition, certain overhead costs also associated with TIF administration are apportioned to all TIF districts and reimbursed to the City.



The TIF administrative allocation process is part of a cost allocation plan guided by federal OMB Circular A-87. This Circular establishes principles and standards for determining costs for federal awards carried out through grants, cost reimbursement contracts, and other agreements with State and local governments and federally-recognized Indian tribal governments (governmental units). While the TIF program is not required to follow A-87, the City has engaged Maximus Consulting<sup>3</sup> to include TIF related administrative costs as part of their overall City cost allocation plan that also provides the City with the calculations required for grant overhead allocations.

The Illinois General Assembly approved language in the TIF Act allowing municipalities the ability to pay themselves for administrative costs. The language established in the Illinois TIF legislation is more restrictive than OMB Circular A-87 in that municipalities are prohibited from billing for administrative costs that would not have occurred if the TIF was not in place<sup>4</sup>.

Relying on the above provision in the TIF legislation and utilizing the methodology established by OMB Circular A-87, \$8,030,527 was charged to TIF districts and allocated back to the City of Chicago as expenditure reimbursement for employees participating in TIF-related projects during 2007 and other related overhead. The TIF administrative allocation includes salaries, overhead, and fringe benefits costs. The total allocated consists of \$4,633,309 related directly to salaries, \$1,766,770 for overhead, and \$1,630,448 for fringe benefits.

## **VII. Audit Expenditure Review - Selection and Examination**

We selected the Central Loop TIF and the Central West TIF for detailed expenditure review. The Central Loop TIF was selected because it was the first TIF established by the City of Chicago and had the most activity of any TIF district. During the selected audit time frame of 2003 through 2007, \$493,106,398 in revenue and \$498,437,499 of expenditures flowed in and out of the Central Loop TIF district. The Central West TIF which had \$37,641,531 in revenue and \$24,331,291 of expenditures during the selected audit period was selected, in part, because the Police Academy in that district was remodeled with TIF funding and the project was managed by City employees. This allowed us to review a completed infrastructure project with many components. The selection of these TIF districts provided us with a diversity of projects and costs encompassing most categories of expenditures allowed under the TIF Act.

In addition to reviewing allowable expenditures, we reviewed the processes, procedures and policies involving porting. We also examined the City methodologies for repayment of TIF money associated with infrastructure expenditures that occurred within TIF districts using non-TIF funds and later repaid to the City, termed transfers.

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<sup>3</sup> Maximus Consulting management has told us they have been handling the City's Cost Allocation Plan in accordance with OMB Circular A-87 for approximately 20 years.

<sup>4</sup> 65 ILCS 5/11-74.4-3 (q) (1.5) After July 1, 1999, annual administrative costs shall not include general overhead or administrative costs of the municipality that would still have been incurred by the municipality if the municipality had not designated a redevelopment project area or approved a redevelopment plan.

Individual expenditures were reviewed based on both judgmental sampling and statistical sampling. Projects were selected to include infrastructure, redevelopment, and inter-governmental.

In our review of individual expenditures, we examined controls established to ensure only eligible expenses as allowed by the TIF Act were authorized and paid, and that the expenditures were classified properly in annual reports published for public review.

In reviewing infrastructure project expenditures, we verified the project budgeted amounts by City departments and compared them to actual expenditures including their eligibility under the TIF Act. Infrastructure reviews included a Loop lighting project on Michigan Avenue from Randolph Street to Congress Parkway initially budgeted from Central Loop TIF funds at \$8,000,000. For the Central West TIF district we reviewed the rehabilitation of the Police Academy located at 1300 W. Jackson Boulevard budgeted at over \$4,000,000 that originally included a draft IGA with the Chicago Park District.

Redevelopment projects were selected from the Central Loop TIF district and Central West TIF district for review. We selected the CNA redevelopment project from the Central Loop TIF district which included verification that developer reimbursements were eligible, promised job opportunities were realized, and contract provisions were appropriate and transparent. In the Central West TIF district we selected the Westhaven Park Homes (WPH) redevelopment agreement that included low income provisions for the purchase of a selected number of condominiums built with TIF funds. Our focus was on verification of the selection and review process for eligibility determination of individuals approved for TIF-subsidized purchases of condominiums.

As part of our review we also examined the payment process to the PBC<sup>5</sup> for projects it was involved in utilizing TIF funding. We selected expenditures from the Central Loop TIF associated with Millennium Park and the Harold Washington College renovation.

Because our review incorporated examination of processes, procedures and internal controls related to TIF disbursements, many other City departments in addition to DCD were also contacted. These departments either received TIF funds for projects, such as Chicago Department of Transportation (CDOT) and Department of General Services (DGS) (infrastructure), or are involved in administrative procedures of TIF funding such as OBM and DOF for porting, transfers, and budgeting of TIF project funds. The review also included the examination of Department of Procurement Services (DPS) policies and procedures relating to contractor adherence to minority/women owned vendor contracting requirements.

In our review process our main objective was not only to verify that TIF funding was expended in accordance with the TIF Act, but to verify that proper internal controls and procedures were in place to provide reasonable assurance that TIF activity was done with transparency and without indication of fraud, excessive waste, abuse, or mismanagement.

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<sup>5</sup> In 1956 Mayor Richard J. Daley formed the PBC to oversee construction and rehabilitation projects for the City of Chicago, Cook County, the Chicago Public Library, Chicago Public Schools, the Chicago Park District and the City Colleges of Chicago. Today, the Board of the PBC is comprised of Mayor Richard M. Daley, who sits as Chair, and ten other business and civic leaders.

## **SCOPE & METHODOLOGY**

The scope of the audit consisted of reviewing selected individual TIF expenditures and expenditures associated with selected projects within the Central Loop and Central West TIF districts for the years January 2003 through December 2007. For certain aspects of the review individual expenditures were also reviewed back to 1997, the first year TIF annual financial reports were required per the State of Illinois TIF Act, 65 ILCS 5/11-74.4-5(d). Field work was completed 09/10/2009.

### **Audit Steps Included:**

- interviewing Department of Community Development, Department of General Services , Office of Budget and Management , Department of Finance, Chicago Department of Transportation, Treasurer's Office, Department of Law, Mayor's Office of Work Force Development, Department of Information Technology (DoIT), Department of Procurement Services, Department of Cultural Affairs, Chicago Police (CPD) and Public Building Commission management, and selected staff participating in TIF activities from these departments and agencies;
- interviewing contractors, suppliers and developers;
- conducting reviews of the following:
  - internal policy and procedures including manuals;
  - applicable rules, laws and regulations;
  - selected developer and IGA agreements;
  - porting and transfer activity;
  - individual expenditures, for compliance with the TIF Act;
- reviewing administrative expenses and allocation methodology;
- reviewing overall compliance with TIF Act reporting and disclosure requirements;

## **OBJECTIVES**

The objectives of the audit were to:

- gain an understanding of the TIF process and purpose;
- determine if expenditures and or activities using TIF funds are legal as defined by the TIF Act;
- determine if TIF projects selected for review are properly monitored and the expenditures or reimbursements are appropriate and without excessive waste, fraud or abuse;
- determine whether TIF funded administrative and /or staff positions are reasonable and appropriate;
- determine if porting TIF funds between districts is in compliance with the TIF Act; and
- determine if transfers of TIF funds are in compliance with the TIF Act;

## **PURPOSE**

The purpose of this review was to assess whether responsibilities were carried out by City management in an effective and efficient manner, with minimal waste, loss, or misappropriation of funds.

DCD management is responsible for the overall administration of processes and internal controls for TIF activities. This includes providing City of Chicago taxpayers reasonable assurance that TIF funds are being spent in compliance with the State of Illinois TIF Act. DCD also has the further responsibility to accurately report TIF fund uses in an open and transparent manner to interested persons as required by Chapter 2-45 of the Municipal Code of the City of Chicago amended by inserting a new Section 2-45-155 TIF Sunshine Ordinance.

OBM and DOF are responsible for oversight of TIF fund transfers and porting. Both departments either separately or together review requests from DCD and other City departments or agencies such as the PBC requesting TIF funds, the disbursement of which may or may not require City Council approval. As part of our review we examined the documentation retained by OBM and DOF which was used in their decision process for TIF fund transfers and porting.

The City's administration of TIF expenditures was selected as an area for review because of the large amount of annual expenditures (\$404,740,806 in 2007), the number of TIF districts (156 as of 2007), and the large TIF Fund balances, totaling \$1,533,251,361 as of 2007 year-end. Additionally, there was a perceived lack of transparency related to TIF expenditures and record retention related to decision making, which made this a desirable area to audit.

#### AUDIT TEAM

Larry Dakof, Auditor  
Wendy Funk, Chief Auditor

## **AUDIT FINDINGS AND RECOMMENDATIONS**

### **FRAUD, WASTE, and ABUSE**

#### **Finding 08-01: Insufficient Monitoring and Reconciliation of Funds and Expenditures Resulted in \$1,202,496.89 in Unused Central Loop TIF Funds Remaining at the PBC for Nearly Three Years**

Due to the way the City sometimes funds projects handled through the PBC, and due to the lack of project fund monitoring and reconciliation, more than \$1.2M in TIF funds went unused and remained in PBC bank accounts.

As part of the TIF expenditure review we selected expenditures paid from the Central Loop TIF district for construction projects managed by the PBC. The two projects selected were the Harold Washington College Rehabilitation with the final payment for work completed in September 2006, and the Millennium Park F-2 Finishes project, final payment for work completed in July 2005.

The Harold Washington College Rehabilitation project consisted of funding from the Central Loop TIF district in the amount of \$38,626,542.99. Expenditures totaled \$37,433,158.57 leaving a surplus of TIF Central Loop funds with the PBC totaling \$1,193,404.42<sup>6</sup> that sat in its bank account for almost three years. These funds should have been returned and could have been utilized for qualifying projects within the Central Loop TIF district.

The Millennium Park F-2 Finishes project managed by the PBC had \$9,092.47 remaining since July 2005 that resulted from the City providing Central Loop TIF district funding totaling \$26,257,346.53 less expenditures of \$26,248,254.06. The total of these two surplus balances, equaling \$1,202,496.89, can no longer be utilized by the City of Chicago because the Central Loop TIF district closed December 31, 2008. To comply with the TIF Act the money must now be returned to the Cook County Assessor for distribution to the various Cook County taxing agencies. This has resulted in the City losing the use of the money that was available for the past two years and could have been used for allowable TIF projects, in the Central Loop TIF district.

#### **Recommendation 08-01:**

We recommend the DOF and OBM work with the PBC to obtain the excess funding paid to the PBC for the Millennium Park F-2 projects and return the money to the Cook County Assessor, as required by the TIF Act, since the Central Loop TIF district is no longer in existence.

Additionally, a review and reconciliation of the funding provided on projects should be performed by the OBM and the PBC to ascertain whether there are balances due the City at

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<sup>6</sup> We have been informed by OBM that as a consequence of our audit finding the City received a check in the amount of \$1,193,404.42 for the excess funds that were held by the PBC in conjunction with the Harold Washington College Rehabilitation project.

specific project intervals. The City should perform these reviews every quarter during the project's life and within a reasonable time frame (perhaps 90 days) of the project's completion.

We also recommend that OBM perform an in-depth review of all projects for which TIF money has been used by the PBC during the past five years to determine if the PBC has retained any funds which should be returned to the proper TIF district or whether any of the funds were used for other projects outside of the originating TIF district and therefore should be returned to the proper TIF fund.

**City Response:**

The Public Building Commission (PBC) acts as the City's general contractor on various City projects. The PBC relies on funding from the City to initiate and complete these projects as it does not have a separate revenue source. Therefore, the City must front funds based on an estimate from the PBC of their cash needs for a period of sixty days.

As noted in the footnote, the City has received the funds from Millennium Park F-2 projects and they have been transferred to the County which has redistributed the funds to the various taxing agencies.

The City agrees that a quarterly reconciliation of cash on hand and estimated expenditures should be performed to ascertain whether there are balances due to the City and will develop procedures with the PBC to implement those reconciliations.

The City does perform final reconciliations on TIF-funded PBC projects after the project is closed out and all project issues have been resolved. That final reconciliation process includes a final determination regarding any TIF funds that are owed to the City. The City will review any TIF-funded projects completed by the PBC in the last five years and complete final reconciliations for any projects that are still open.

And while there are certain issues that can delay completion of a final reconciliation – such as legal and insurance matters – going forward, the City will work with the PBC to perform final reconciliations in a more timely fashion.

**Finding 08-02: The PBC Improperly Paid to the Department of Cultural Affairs \$329,000 in Central Loop TIF Funds for the Purchase of Public Art, a Non-Eligible Expense, in Violation of the TIF Act.**

In October 2007 the DCA invoiced the PBC \$329,000 for “Public Art to be incorporated into the project to renovate the Harold Washington College building, pursuant to the City’s Public Art Ordinance.” The PBC, acting in its capacity as project manager, paid the DCA invoice with funds from the Central Loop TIF for what was in fact a cost that was ineligible for TIF funding.

The City of Chicago established a program known as the Public Art Program under Municipal Code § 2-92-070 (Prior code § 26-7.1; Added.Coun.J. 7-29-87, p. 2826; Amend. 3-10-99, p.91075). Section 2-92-090 states “Every budget for the construction of or renovation affecting 50% or more of the square footage of a public building to which there is or will be public access built for or by the City of Chicago and every budget for a City of Chicago outdoor site improvement project to which there will be public access and that has been designated an eligible public art program project by the public art committee shall provide that 1.33 percent of the original budgeted cost of construction or renovation of the structure or the project itself, excluding land, architectural design fees, construction management and engineering fees, fixtures, furnishings, streets, sewers and similar accessory construction, shall be appropriated and deposited in the public art program fund as specified in Section 2-92-120 , to commission or purchase artwork to be located in a public area in or at such building or project; *provided, however, this provision shall not apply to any building or project constructed with funds which exclude public art as an eligible cost.*” (Emphasis added.)

We sent a letter to the Commissioner of the DCA requesting all documentation supporting artwork purchased for the Harold Washington College. In response to our request the Commissioner indicated in a letter that no artwork had been purchased or installed at Harold Washington College and the only documentation available was a copy of the check for \$329,000 sent from the PBC to the DCA.

The TIF Act as amended in 1999 does not list artwork as an allowable TIF expenditure. Therefore this expenditure violated the TIF Act.

Additionally, in an e-mail sent to the OBM in January 2008, the City’s Law Department stated that “The cost to purchase and display public art at a public school facility does not fit within a TIF eligible redevelopment project cost category under the TIF Act.” The Law Department further indicates “If public art is to be acquired and displayed, it would be voluntary and *presumably would have to be funded from other than TIF revenues.*” (Emphasis added.)

While this specific email from the Law Department was in response to spending TIF dollars on renovations at Chicago Public Schools, the facts would apply to all redevelopment projects and moveable<sup>7</sup> artwork would always be excluded as an allowable TIF expenditure.

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<sup>7</sup> Moveable artwork is art work that can be removed from the facility. It is not permanently affixed such as a mural or mosaic.

It appears that neither the PBC nor the DCA were aware that TIF Funds could not be used for this type of expenditure. Additionally, no reconciliation or review of expenditures was done by the City's OBM which allowed this error to occur and go undetected.

**Recommendation 08-02:**

We recommend that DCA return the \$329,000<sup>8</sup> that was paid to them by the PBC since the Chicago Municipal Code Public Art Work Ordinance does not apply to TIF funded projects. The DCA should also be informed that any projects funded by TIF are ineligible participants and are not subject to the Public Art Ordinance. The OBM must review all charges associated with expenditures using TIF funds to be certain they are in compliance with the Act. Additionally, since the Central Loop TIF is no longer in existence, the \$329,000 should be turned over to the Cook County Assessor for distribution to the proper taxing districts as required by the TIF Act.

**City Response:**

The City agrees with the recommendation and, as noted in the footnote, monies have been received by the City from the PBC and transferred to Cook County, which has redistributed the funds to the taxing agencies.

When projects are established utilizing TIF funds, OBM does review the planned expenditures to determine compliance with the TIF Act.

This project, however, was initially budgeted to utilize general obligation bond proceeds and therefore was subject at that time to the Public Art Ordinance. However, as the funding source for the project was changed to TIF, the Public Art Ordinance would no longer apply.

In this case, planned expenditures should have been reviewed again to ensure compliance with the TIF Act. Going forward, when funding sources are changed to TIF, the City will ensure that planned project expenditures are reviewed by OBM to ensure compliance.

Finally, earlier this year, OBM, under the direction of the Chief Financial Officer, assumed responsibility for managing and monitoring all TIF funds and accounts. This important realignment of responsibility should greatly strengthen the oversight of TIF expenditures in all areas, including those made by the PBC.

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<sup>8</sup> Subsequent to IGO disclosure of this issue incident to the execution of this audit, we were informed that the DCA returned the money to the PBC and that the PBC will return the money to the City.



**Finding 08-03: \$54,266.26 in Contractor Assessed Liquidated Damages Due the Central West TIF Have Not Been Collected**

The Police Academy remodel had 16 Job Order Contracting (JOC) sub-orders placed with two general contractors; nine sub-orders with Paul Borg and seven sub-orders with Old Veterans. In our review of the sub-order Compliance Assessment memorandums associated with these 16 sub-orders we obtained documentation from DPS indicating that \$61,539.07 was due from these contractors to the City for non-compliance within the following categories: Minority Journeyworkers, Female Journeyworkers, Minority Apprentice and Female Apprentice, Minority Laborer, Female Laborer, and the Chicago Residency Ordinance.

Of the \$61,539.07 due for assessments, \$54,266.26 represents money due back to the Central West TIF since the sub-orders associated with this portion of the assessment were paid from TIF funds. The remainder, totaling \$7,272.81, is non-TIF related funding due back to the City. When we contacted DGS to determine when the funds were repaid and what account they were deposited in we were told that no money has been collected.

DGS informed us that they do not attempt to collect deficiencies based on individual sub-orders of a master contract but instead wait until DPS provides an assessment report for an entire contract which is made up of many sub-orders.

When we asked about the assessment report for the entire contract DGS indicated that they have not received one from DPS in over a year and as a result did not know what amount to withhold from the contractor for assessment deficiencies. DGS produced a memo dated March 20, 2009 written to the Assistant Deputy Procurement Officer from the Deputy Commissioner DGS asking for final assessment reports on expired or expiring contracts. As of August 20, 2009 no reply was sent in response to the DGS March 20, 2009 memo.

DPS management informed us that they had not sent out final contract assessment letters because they were not being kept up to-date from DGS regarding final close out of projects and therefore unable to issue final assessment information.

In response to letters DPS sent to Paul Borg regarding assessments for sub-orders associated with the Police Academy, Paul Borg responded with a letter to DGS indicating they did not owe any deficiencies since no funds were withheld prior to final payment of their master contract which had since expired prior to them receiving requests for the assessment. DPS subsequently responded to Paul Borg indicating the assessment is valid and due.

Good business practices would require that a process for timely review and retention/collection of non-compliance assessments be in place and that all City departments understand their role in working with DPS to ensure the funds due the City are retained prior to final contractor payments.

The impact of not having a good process in place has resulted in funds being paid out to vendors when in fact the funds should have been retained by the City.

**Recommendation 08-03:**

We recommend City departments using the JOC system be required to notify DPS of project completions within 90 days. All relevant documentation required by DPS to close out contracts should be included with the notifications. In addition, City departments using JOC should maintain an up-to-date record of contractor cumulative assessments and amounts due contractors from open projects ensuring that the City has retainage to cover all deficiencies assessed. DGS in conjunction with DPS should contact Paul Borg regarding the disputed amounts due from the Police Academy sub-orders to resolve the issue.

**City Response:**

The City agrees with parts of this recommendation.

The Department of Procurement Services (“DPS”) has sent a memorandum to all City departments using the JOC system instructing them to notify the Office of Compliance (“OCX”) of project completions in a timely manner and to provide all relevant documentation needed for close-out (OCX is responsible for project close-outs and monitoring of EEO and CRO requirements). DPS instructed departments to maintain up-to-date records of contractor cumulative assessments and amounts due contractors from open projects ensuring that the City has retainage to cover all deficiencies assessed.

Procurement finalized the cumulative assessments for Paul Borg and Old Veteran Construction (OVC). Procurement will transmit those assessments for departments using JOC contracts to OCX.

DPS sent the final closeout letter for the OVC and Paul Borg JOC Contracts to DGS and the Contractor. The final closeout letter for Paul Borg included the disputed amounts due from the Police Academy sub-orders. On March 19, 2010, counsel for Paul Borg filed a protest with the City regarding the matter. DPS, with Law’s input, has settled the Paul Borg closeout issue in an amount of \$84,941 and has received a check in the amount \$57,305 from Paul Borg and cancellation of the final invoice in the amount of \$27,635.

However, the City strongly disagrees that the liquidated damages must be returned to the TIF. The contractor's damages can legally be considered to have lost any characterization as TIF funds. The liquidated damages are assessed after the contract's completion. Funds paid or payable to the contractor under the contract belong to the contractor and are no longer TIF funds. It is from funds that belong to the contractor that the liquidated damages are paid.

And in fact, the City’s resident hiring ordinance requires that residency damages be used to establish worker training programs. Section 2-29-330 of the Municipal Code of Chicago, subsection (e) thereof provides that “(e) The monetary damages stipulated in subsection (b) hereof shall be used for establishing a worker training program.”

In this case, the City intends to allocate all of the \$84,941.81 toward worker training programs.

But going forward, as a matter of policy, we will consider whether in certain cases, when legal and appropriate, liquidated damages can be reallocated to TIFs.

### **IGO Response to City Response:**

We strongly disagree with the portion of the City's response suggesting that the contractor's damages as paid or charged can legally and legitimately be considered to have lost any characterization as TIF funds that can be spent to pay TIF eligible redevelopment project costs under the TIF Act. The Law Department presumes that the simple fact of contractor completion of the project and consequent entitlement to payment for contract work *actually performed* somehow cleanses the portion of the disbursement constituting overpayment of its TIF originated character.

By taking the above position the Law department fails to recognize that TIF funds are the source of the contractor payment and therefore subject to Illinois TIF legislation. The Law Department is suggesting that if a contractor is overpaid for services and has to reimburse the City, the money is no longer TIF-related and does not have to be returned to the TIF district. The Law Department is contending that TIF funds are, in essence, cleansed of their TIF origins by the City's overpayment to contractors beyond what the contractors were legally owed. We strongly disagree with this interpretation. The fact that the contractor violated conditions of the contract reduced the amount owed to the contractor, and therefore reduced the amount that should have been paid from TIF funds. The full payment was effectively not owed to the contractor, and would not be shown as expenditure in the TIF district's financial statement and therefore should remain in the TIF district fund balance. Moreover, the Law Department's response further neglects the fact that TIF funds are derived from property taxes that otherwise would be disbursed among eight taxing districts, the City being just one of the eight. (If the funds are not returned to the TIF, as we believe should be the case, then minimally, they should be equitably and proportionally distributed to the eight taxing districts.)

In addition the Law Department indicates that under the City's resident hiring ordinance provisions (Section 2-29-330 of the Municipal Code of Chicago), subsection (e) thereof provides that "(e) The monetary damages stipulated in subsection (b) hereof shall be used for establishing a worker training program." We do not disagree that the Skill Builders Program is a training program, but, it is outside of the TIF district from which the TIF funds came and is therefore ineligible as a TIF expenditure. Since the Illinois TIF Act requires the training program to be within the TIF district where the funds are disbursed and the Skill Builders Program is outside of the TIF district the training program is an ineligible expenditure. In this case the Illinois TIF Act supersedes the City of Chicago Municipal Code and makes this point moot.

**Finding 08-04: Employees of DGS Engaged in Deceptive Billing Practices in Conjunction with Old Veterans Construction and Paul Borg Construction in Transactions Involving the Use of TIF Funds**

DGS allowed Old Veterans and Paul Borg Construction to submit misleading billing documentation from the JOC system to the City for the acquisition of products that were materially misrepresented on the billing used to substantiate payment.

The Police Academy renovation consisted of 16 sub-contracts which made up the detail of supplies and material purchased through the JOC system. We reviewed these sub-contracts or billing detail and found three instances where the quantity and description indicated on the billing detail did not match with the quantity description provided for the materials being purchased.

In the first instance under sub-order JB5-029G, 8.62 was the quantity listed for the purchase of Chemical Toilet, Small Tank 7000 Uses/Year. There is an additional description listed below the quantity as “Temporary Showers.”

The second instance listed 2.20 under sub-order JB5-029H as the quantity and Portable Basketball Backstop with Rim, as the description.

In the third instance sub-order JB5-029C showed the quantity was .80 with a description of Horizontal Ladder and an additional description of “Supply only one Ball Tree ½ base with 6 arms.”

When we brought this to the attention of DGS management we were informed that the quantity was manipulated to arrive at a total dollar amount coinciding with the purchase of items not in the JOC system but using the prices and descriptions of items in the JOC system to match the dollar amount of the actual items purchased as a method to avoid the normal procurement process.

We received the following support for the noted purchases: 1) an invoice from Service Sanitation for temporary showers that were used at the site while the shower rooms were being remodeled 2) an invoice from Porter Athletic Equipment for basketball backstops but the invoice did not match with the dollar amount charged through the JOC system 3) an invoice for a fitness ball tree ordered from Australia with shipping costs more than half the cost of the tree. The invoice was also in Australian dollars and does not appear to have been converted to US dollars resulting in an overcharge to the City of \$573.63 in addition to the manipulation of the JOC system.

As part of the Police Academy review we prepared a schedule of 33 JOC billed items for physical verification selected from 12 out of the 16 JOC sub-contracts totaling \$686,287.62. During verification at the Police Academy we determined that six LCD Samsung 32 inch TV’s were installed in the Police Academy exercise room. We reviewed each JOC sub-contractor detailed billing and could not locate under which detailed JOC billing these TV’s had been purchased. When questioned about the purchase DGS management explained the following:

Under sub-order JV5-085A, the original scope of work called for Audio and Video changes & modifications that included installing new Fiber Optic feeds to a proposed computer center located on the second floor. Originally, DGS was going to install CPD supplied video monitors in the exercise room. The project scope changed, eliminating some of the Fiber Optic costs and creating a credit due the City of Chicago. Instead of revising the JOC billing, DGS kept the original billing listing the Fiber Optic supplies and had the contractor use the credit to purchase TV's.

By not revising the JOC billing, DGS and the contractor distorted the billing so that anyone reviewing the detail of items purchased would not be able to understand that items listed on the JOC billing such as Fiber Optic Direct Burial Cable, 48 Strand, quantity 2 at \$2,530.00, Fiber Optic Modem, Range 3 Miles, 12 Channel, 1 at \$1,895.26 and Fiber Optic Splice Box-Manholes, 1 at \$3,579.49 were in fact used to acquire the six 32 inch LCD TV's.

The practice of substituting items billed for the purchase of other items completely destroys the integrity of the JOC system. Since the JOC detail is used to support the invoicing by the contractor, Old Veterans and Paul Borg were perpetrating deceptive billing practices by submitting documentation that they knew was inaccurate. DGS also committed deceptive billing practices by acting in concert with Old Veterans and Paul Borg by providing inaccurate documentation that purports to have received materials or services that were being billed to the City yet never received. Without further in-depth review that is beyond the scope of this audit it can not be determined how many other substitutions may have taken place and what those substitutions might have been. By manipulating the JOC system in the manner described above it is impossible to determine if DGS substituted other line items that resulted in materials which were never used at the Police Academy.

It should also be noted that within DGS, the JOC payment approval process does not require review of receiving documents against items billed through the JOC detail. This lack of proper internal control allowed for the situations noted to occur and go unnoticed by those processing payments.

#### **Recommendation 08-04:**

We recommend that written policies and procedures be established by DPS to provide guidance to users of the JOC system for approved and acceptable methods to acquire goods or services not listed in the JOC catalog that are infrequent or one time purchases. All JOC users and contractors should be notified that manipulating quantities of JOC catalog listed items in order to produce a dollar total for the purchase of another commodity or service other than the one listed in the JOC catalog as a method of procuring one time purchases is prohibited, and as a consequence, contractors may risk losing status as an approved City supplier. The Gordian Group<sup>9</sup> should be consulted to set up procedures and system controls disallowing quantities that are not rational for the item being purchased.

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<sup>9</sup> The Gordian Group is a private company contracted by the City to maintain the JOC system which is an electronic catalog of frequently acquired services and materials used by various City departments for construction project ordering. The Gordian Group fee for maintaining the JOC data base is 1.5% to 2% of any purchases acquired through the JOC system.

Additionally, we recommend that DGS initiate a review process through the DGS Finance Section to require that signed receiving documents be submitted to and matched against the JOC billing detail prior to processing for payment. Invoices containing JOC line items not able to be matched against signed receiving documents should not be paid until they are investigated to determine their validity.

This matter has also been referred to the IGO Investigative section for possible review.

**City Response:**

The City disagrees that DGS employees acted in concert with contractors to engage in deceptive billing practices. However, the City does agree that the “change order” process should have been utilized and was not. DGS disciplined the employees involved in the project for not following the change order process.

JOC policies and procedures already contain a specific procedure for acquiring items not listed in the construction task catalog. DPS has redistributed those written policies and procedures and has worked with the Gordian Group to conduct training for users of the JOC procurement method. The training focused on a variety of critical JOC matters, including using the non pre-priced procedure / acquiring items not listed in the construction task catalog.

However, it is important to note that DGS complies with payment procedures established in Section XIII of the Terms and Conditions for JOC purchases.

**IGO Response to City Response:**

DGS employees directed contractors to substitute items without changing the actual billing submitted to the City of Chicago. In addition these same employees approved the billing certifying that the items shown were in fact received. This apparent intentional manipulation of the billing destroys the billing integrity and hides the true nature and quantity of the products being acquired which constitutes deceptive billing practices.

**Finding 08-05: \$89,753.74 of Central West TIF Money Was Spent on Questionable Expenditures**

Although the Chicago Park District did not end up participating in the Police Academy renovation project, their specifications regarding renovation of the gymnasium caused \$89,753.54 in questionable and unauthorized expenditures.

In 2006 an initial budget of \$2,000,000 was established from Central West TIF District funds along with an equipment note in the amount of \$250,000 of non-TIF money to renovate the Police Academy located at 1300 W. Jackson Blvd. In April of 2007 additional funding for \$2,000,000 more in TIF money was requested by the DGS for additional project work making the total budget from TIF funds \$4,000,000.

In June of 2007 an IGA between the City of Chicago and the Chicago Park District was drafted and circulated within the Park District, Police Department, and City of Chicago. The agreement was to allow the Chicago Park District (which owns the land on which the Police Academy is located) use of the Police Academy gymnasium on weekends and evenings. The Park District was to provide \$750,000 in funding for project renovations associated with its use. In return for the funding the Park District required certain specifications, materials and renovations unique to their participation. Documentation provided by DGS indicates that certain work including gymnasium flooring specified by the Park District in the amount of \$194,753.74 was installed. Additionally, certain other design and consulting fees totaling \$15,000 related to the Park District use of the Police Academy were incurred prior to obtaining an executed IGA approved by City Council Ordinance. DGS provided the IGO auditors with cost estimates of \$120,000 for the Police Academy gymnasium floor if the Park District specifications were not used. The difference in the actual cost of \$194,753.74 for the Park District specified floor and \$120,000.00 for the floor prior to the Park District inclusion is \$74,753.74 plus the \$15,000 in additional Park District design costs total to \$89,753.74 in questionable expenditures of TIF funds.

In our review of documents obtained from DGS we found e-mails from the DGS Project Manager to OBM and the Mayor's Office requesting budget approval for the additional costs being incurred for the Park District's use of the Police Academy Gym. We did not find any documentation from OBM or the Mayor's Office instructing DGS to halt any further construction or design costs associated with the Park District.

Costs related to the Police Academy IGA should not have been incurred until there was an agreed contract approved by the City Council and the Park District Board. In the case of the IGA between the City of Chicago and the Park District this agreement never made it past the first stage of discussion points. There never was a consensus formed as to the basis of the terms and conditions when DGS was spending TIF funds in anticipation of the Park District and the City agreeing to the contract terms. There never was authorization by the City Council approving this project and the appropriation of funds, which is required for all IGAs.

**Recommendation 08-05:**

We recommend that future TIF funded projects not move forward until all terms agreed to by all participants are in writing, signed by all parties, and approved by the City Council when required. We recognize the urgency at times to move construction projects along, but in the absence of proper authorization by the appropriate legislation we recommend that money associated with IGAs is not committed until approved by the City Council.

**City Response:**

The City disagrees that Central West Loop TIF money was spent on questionable expenditures. The hardwood floors incorporated into the design of the police gymnasium were determined to be more cost effective than the original design plan for the synthetic floor. Hardwood floors can last from 30-40 years because they can be refinished multiple times. On the contrary, synthetic floors last 15-20 years and cannot be refinished. In this case, it was the right decision to install hardwood floors because of their durability and long term cost effectiveness, whether or not the Chicago Park District participated in the project.

However, the City does agree that terms of TIF-funded projects and the required agreements that dictate those terms must be signed and executed before construction moves forward.

But in this case, the City made the decision to install the hardwood floors regardless of the Park District's participation.

**IGO Response to City Response:**

Whether the City's proffered analysis of the cost-effectiveness of hardwood floors is in fact correct, we cannot say. What we can say is that the City's response advances a rationale not anywhere reflected in the underlying documentation supporting the project as executed. It therefore appears to be a post-hoc rationalization for what, on the basis of the record, appears to be a significant expenditure undertaken without proper authorization.



**Finding 08-06: Liquidated Damages Were Used in Violation of the TIF Act to Fund Ineligible Training Program Expenditures of almost \$85,000 to a Program Outside of the TIF District**

In our review of the Harold Washington College Renovation and the Millennium Park F-2, Park Finishes, Landscaping and Arcade projects we determined that the general contractors for these two projects, Pacific Construction and McHugh/Riteway Joint Venture, were assessed damages for non-compliance with residency and economic opportunity goal requirements. When we requested information regarding the disposition of the recovered damages we were informed by the PBC that the money in both of these instances was used to fund a jobs training program called the “Skill Builders Program”.

The “Skill Builders Program” is an apprenticeship preparation program that helps City residents to obtain basic skills to successfully take the exams and enter apprenticeships in the trades. An IGA between the City of Chicago and the PBC was established April 29, 2005. The IGA established the MOWD as the controlling entity for design and format of programs that will be funded from liquidated damages assessed against contractors on PBC projects. The City, through the MOWD, entered into a Delegate Agency Grant Agreement with the Construction Careers Council of Ace Tech called “The Skill Builders Program” whose offices are located at 5410 S. State Street, Chicago, IL. The Delegate Agency Grant Agreement provides for \$400,000 per year funding from the City which will be accumulated by the PBC from the liquidated damages account.

Prior to the establishment of the IGA in 2005 the PBC was the administrator of the Skill Builders Program, remitting the money collected from liquidated damages to the program. Between 2001 and 2009 records from the PBC indicate that \$4,074,939.81 was collected for liquidated damages. We did not verify liquidated damage payments made by the PBC to the Skill Builders Program prior to 2005. We did verify that the PBC remitted to the City offices of OBM and MOWD \$1,600,000 between 2005 and 2009. What cannot be determined, and was not within the scope of this audit, is where the sources of all the funds, TIF or non-TIF, related to the individual projects came from. If the funds for the projects were related to TIF funding and the TIF districts were outside the district from which the Skill Builders Program operated then the money was an ineligible use and should have been returned to the TIF districts funding the projects.

Liquidated damages were assessed against Pacific Construction under contract #1308 for the Harold Washington College Renovation in the amount of \$11,486.23 due to non-compliance with the City of Chicago residency requirements. In our review of the expenditures we were unable to determine if and when the \$11,486.23 was returned to the City and refunded to the Central Loop TIF district. Since all Harold Washington College Renovation expenditures under contract #1308 paid to Pacific Construction were paid out of Central Loop TIF funds any assessed damages should have been returned to the fund. In our inquiry as to the disposition of the liquidated damages we were informed by the PBC that the money was used for a job training program called “Skill Builders Program”.

Liquidated damages were also assessed against McHugh/Riteway Joint Venture under contract #1303 for the Millennium Park F-2, Park Finishes, Landscaping, and Arcade project in the amount of \$73,395.93 due to failure to meet economic opportunity goals. This assessment also was not returned to the Central Loop TIF district but was distributed by the PBC to the Skill Builders Program.

The PBC provided a memo dated 3/24/2006 to OBM indicating that payment of \$400,000 representing the second installment check of three \$400,000 payments from the Skill Builders liquidated damages fund would be forwarded to the City. Part of the \$400,000 transfer was made up of these TIF funded liquidated damages, as described above.

The TIF Act 65 ILCS 5/11-74.4-3(q)(5) specifies that “Costs of job training and retaining projects, including the cost of ‘welfare to work’ programs implemented by businesses located within the redevelopment project area” are TIF eligible. The Skill Builders Program is located at 5410 South State Street clearly outside of the Central Loop TIF area and therefore not an eligible TIF expenditure and thus violated the TIF Act.

It appears that the payment of ineligible expenditures was caused by the lack of procedures at the PBC, DCD, and the OBM to monitor for TIF eligible expenditures from liquidated damages related to TIF funded projects.

#### **Recommendation 08-06:**

We recommend that since the Skill Builders Program does not meet the TIF eligible guidelines for use of Central Loop TIF funds, the \$11,486.23 and \$73,395.93 be returned by the PBC to the City and then returned to the Cook County Assessor since the Central Loop TIF District is closed. Additionally, decisions to use TIF funds must be reviewed by competent persons familiar with TIF Act requirements. Programs such as the Skill Builders Program must be reviewed for funding sources on a continuous basis. No funds should be transferred without having proper reviews and sign off from DCD personnel familiar with TIF requirements. This documentation must then be retained in the project files at the PBC, OBM, and DCD. Additionally, the OBM needs to determine if a review of all sources of funds associated with liquidated damages remitted to the Skill Builders Program should be analyzed. If it is determined that money paid by the PBC for the Skill Builders Program came from TIF funding outside the TIF district in which the Skill Builders Program is located, then the funds must be returned to the proper TIF district.

#### **City Response:**

The City strongly disagrees with this finding and the assertion that liquidated damages collected from contractors must be returned to the TIF.

As referenced in finding 08-03, the contractor's damages can legally be considered to have lost any characterization as TIF funds. The liquidated damages are assessed after the contract's completion. Funds paid or payable to the contractor under the contract belong to the contractor

and are no longer TIF funds. It is from funds that belong to the contractor that the liquidated damages are paid.

And in fact, the City's resident hiring ordinance requires that residency damages are used to establish worker training programs. Section 2-29-330 of the Municipal Code of Chicago, subsection (e) thereof provides that "(e) The monetary damages stipulated in subsection (b) hereof shall be used for establishing a worker training program." The Skill Builders Program is such a program.

But going forward, as a matter of policy, we will consider whether in certain cases, when legal and appropriate, liquidated damages can be reallocated to TIFs.

**IGO Response to City Response:**

See IGO Response to City Response in Finding 08-03.

**Finding 08-07: Fitness Equipment Purchased for the Police Academy Workout Room Resulted in \$39,773.99 of Wasted TIF Funds and Two 32 Inch Flat Screen TV's Valued at approximately \$577<sup>10</sup> each were Stolen by an Employee of the Ordering Contractor**

Improper use of the JOC purchasing system and lack of monitoring by project managers during the Police Academy renovation resulted in wasted funds and unaccounted for items.

Part of the Police Academy renovation included remodeling and expanding the existing workout room used by Police Academy staff, City of Chicago police officers and police cadets. The remodel included the replacement of workout equipment that was over ten years old. DGS Project Managers worked with Police Academy staff to develop equipment requirements and specifications for the new equipment that was purchased.

Upon determining the equipment specifications DGS contacted two suppliers, LifeFitness and Direct Fitness Solutions, Inc. LLC to obtain bids for the purchase, delivery and installation of the fitness equipment. After DGS obtained the bids The Gordian Group was requested by DGS and the general contractor (Old Veterans) to add the fitness equipment specified by the Police Department into the JOC system electronic catalog. Gordian would obtain bids (in this case DGS already obtained pricing) and submit the bid pricing to the DPS for review and approval for inclusion into the JOC catalog.

After the equipment pricing was approved by DPS and included into the JOC system DGS ordered the equipment using the JOC system. Old Veterans then ordered the equipment for DGS directly from LifeFitness and Direct Fitness Solutions, Inc. LLC. The cost to DGS was based on the JOC price catalog. Old Veterans was paid an 18.05% markup from the prices listed in the JOC system and The Gordian Group was paid a 1.5% fee based on the JOC price. Together these resulted in a 19.55% additional cost using the JOC. The documentation we reviewed determined that DGS effectively bid the equipment out and obtained the pricing. DGS should have acquired the fitness equipment using DPS procurement processes as outlined in the City of Chicago Procurement Policy and Process Manual. They then could have obtained the equipment directly from LifeFitness and Direct Fitness Solutions, Inc. LLC instead of through the JOC system saving the TIF the 19.55% markup.

In our review of JOC costs we independently contacted both equipment providers LifeFitness and Direct Fitness Solutions, Inc. LLC and requested copies of invoices they sent to Old Veterans Construction and found (1) sales tax<sup>11</sup> totaling \$4,813.73 was charged to Old Veterans from Direct Fitness Solutions, Inc. LLC that was incorporated into the JOC prices and (2) using the JOC process instead of procuring through DPS cost the TIF an additional 19.55% representing the contractor markup and the Gordian fee, or \$34,960.26.

Based on our analysis, using the JOC system instead of purchasing the fitness equipment directly from the two suppliers through DPS cost the TIF district \$39,773.99 which is the total of (1) and (2) above.

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<sup>10</sup> Prices were obtained by averaging 3 listed prices for 2009 VISIO 32 inch televisions currently listed on the internet for sale.

<sup>11</sup> The City is a government entity and therefore purchases should be tax exempt.

In our interviews with DGS we inquired as to the reason why the fitness equipment was not ordered directly by the City through DPS saving the contractor markup of 18.05% and the Gordian fee of 1.5%. We were told that DGS was originally intending to use DPS but after obtaining CPD's specific equipment requests it was not possible to use DPS because multiple suppliers were required and they were under time constraints to finish the project quickly.

We determined that the old equipment was still functional since it was redistributed to other City locations thus removing the argument that there was an immediate need and time was a constraint requiring DGS to avoid using DPS and the normal procurement processes.

As part of our review of TIF expenditures purchased using the JOC system we selected various items purchased by the general contractors to verify their existence and description against the actual billing. When we reviewed the actual invoice sent by Direct Fitness Solutions, Inc. LLC to Old Veterans Construction we discovered the existence of two 32 inch Visio flat screen TV's at no charge shipped to the Police Academy as promotional items. We determined that the TV's value based on 2009 pricing should be around \$577 each or \$1,154 for the two.

In our inventory verification we were unable to locate the two 32 inch Visio flat screen TV's at the Police Academy.

We were informed by the DGS Police Academy Renovation Project Manager that he had no knowledge of the TV's and did not know they were shipped to the Police Academy. Staff at the Police Academy also had no knowledge of the TV's existence. Police Academy staff assured us that the two TV's were never installed at the Police Academy nor were they ever transferred to another facility. We additionally talked to the Police Academy Electrician who would have been the individual responsible for their installation and he also verified that the TV's were never installed.

The information we obtained regarding the missing TV's was provided to the Inspector General's Investigation section. IGO investigators subsequently determined from interviews with employees of Old Veterans that the TV's were never turned over to the City but instead were kept for their own personal use<sup>12</sup>. Since these TV's were promotional items obtained from purchases using City funds the TV's were City property and should have been used at the Police Academy to offset costs of TV's purchased for the facility.

Good internal controls would require that project managers understand when to use the JOC system and when to use the normal City procurement process through DPS in order to ensure the City receives the best possible pricing under the circumstances of the purchase. In this case, it appears that time was not truly an issue and that DGS had already effectively obtained bids themselves leaving the middle man (Gordian) with nothing to do in the process but earn its fee. Additionally, the DGS project manager had no role in reviewing documentation for receipt of goods at the project site and therefore did not monitor whether all goods shipped were received

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<sup>12</sup> The IGO Investigation Section conducted a separate investigation of this matter and reported out its findings and recommendations to the Mayor.

and properly used for the project. This also represents a lack of proper internal control in monitoring the project.

**Recommendation 08-07:**

We recommend a process be put in place to ensure that when items or services not included in the JOC catalog that are of a non-recurring nature are needed and time is not a significant factor, DPS be brought into the process at the very early stages of budget development to assist the departments in obtaining the products and services through the City of Chicago Procurement Policy and Processes outlined in its manual. DGS had ample time to involve DPS in the procurement process; they worked with the Chicago Police Department in developing the specifications which could have been submitted directly to DPS.

We also recommend that project managers obtain delivery documents from the general contractor and verify independently that the items listed as being delivered are accounted for. The project manager should also maintain a file documenting who received the items and when they were received. We further recommend that all contractors placing orders using the JOC system be notified by DPS that any promotional items provided on orders placed on behalf of the City of Chicago are the property of the City and must be turned over to the City.

**City Response:**

The City disagrees with the recommendation.

In this case, DPS authorized the use of the JOC procurement method. DGS then followed the “Non Pre-Priced Work Requirements” contained in DGS’ JOC contract General Conditions (December 2006). Section 5(b)(4) states in part:

*At the discretion of the City, Non Pre-priced tasks as well as other tasks may be added to the CTC (Construction Task Catalog) during the course of the Contract. Upon mutual agreement between the City and the Contractor, unit prices will be established based on actual quotes from material suppliers and installers and fixed as a permanent task in the CTC. (Department of General Services JOC General Conditions, pg 123)*

For payments to contractors, DGS complies with Section XIII of the Terms and Conditions for JOC Construction contracts which details billing procedures for contractors. It does not include any requirements for obtaining delivery tickets from the general contractor. Rather, DGS project managers review construction drawings, specifications, and the line items listed in the proposal, including quantities, to ensure the contractor has provided all that was contracted and paid for.

Regarding the other specific claims and recommendations:

Old Fitness Equipment

It is an inaccurate claim to say that there was no “immediate need” for the equipment simply because the old equipment was still functional. In fact, DGS always strives to recycle all City

materials (furniture, cubicles, equipment, etc.) whenever possible. In this case, since the “old” fitness equipment was functional, it was moved to another police facility and is currently in use.

However, the old equipment could not be used in the new space because of differing space and power requirements, so there was indeed an immediate need for the new equipment.

“Lack of Monitoring By Project Managers”

DGS project managers review construction drawings, specifications, and the line items listed in the proposal, including quantities, to ensure the contractor has provided all that was contracted and paid for. In this case, every piece of fitness equipment that was part of the scope was delivered, installed and accounted for. A project punch list is also developed to rectify uncompleted or unsatisfactory work items owed to the project.

Missing TV's

DGS employees were not aware of the promotional offer given by the vendor. In fact, they did not become aware until the IG audit was conducted. DGS agrees the TVs are the property of the City of Chicago. DGS sought and received reimbursement in the amount of \$1,440.00 from Old Veteran's Construction.

DPS notified City Departments that any promotional items provided on orders placed on behalf of the City are the property of the City and must be turned over to the City.

**IGO Response to City Response:**

The fact that the City followed authorized JOC procurement methods does not relieve it of its responsibility to utilize fiscal prudence and common sense. Since DGS employees developed the equipment specifications in conjunction with the Police Department and they obtained equipment proposals that were utilized by the JOC contractors we believe it would have been in the best interest of the City and the taxpayers for DPS to have ordered the equipment saving the TIF district \$39,773.99. The equipment could have been ordered and received well in advance of its installation date, thus obviating any concerns about an "immediate need" for the fitness equipment.

**Finding 08-08: Costly Material Selections for the Police Academy Wasted \$18,297**

Some materials were selected for purchase based on aesthetic reasons rather than functionality resulting in waste of taxpayer dollars in the Police Academy renovation project.

Part of the renovation of the Police Academy included remodeling and expanding the existing workout room used by staff, police officers and cadets. As part of the renovation in the workout room a dividing wall was erected and decorated with Terrazzo tiles costing \$23.43/SF for a total of \$11,997.66. When we toured the Police Academy we inspected the workout room and found this wall in the cardio exercise area of the gym. We did not find any peculiar circumstances that would require such ornate materials especially since this is a workout room not open to the public. We believe this wall could have easily been painted at a cost of \$1.13/SF or \$578.56 which is based on the cost of painting surfaces in other locations of the Police Academy saving the taxpayers and the TIF district over \$11,419.10 just in the decoration of this one 512 SF dividing wall.

There were three drinking fountains installed *inside* the Police Academy at a cost of \$2,730.94 each. The drinking fountains were specified to be *outside* drinking fountains with bubblers. When we reviewed alternative selections in the JOC catalog we found a white two-station indoor enameled drinking fountain with bubbler for \$1,271.34 at 2009 pricing. Had the alternative drinking fountain been chosen the per unit cost reduction including Gordian fee and contractor markup would have been \$1,854.59 or a \$5,563.77 savings for the three fountains.

A chrome fitness ball tree to store rubber fitness balls was ordered from Australia by the contractor Paul Borg. The price paid by the TIF district for this item was \$759.50 not including shipping, contractor markup and Gordian fee. The shipping cost for this ball tree from Australia added 52% more to the cost or \$392.25. Adding up all the costs for this item cost the TIF \$1,314.62. Additionally, the supplier was paid in US dollars when in fact the invoice was in Australian dollars that should have been discounted approximately 17% for the conversion. Although this was not a large dollar amount, the item purchased was an unreasonable and unneeded expenditure. Based on discussions with DGS, this item was chosen for design. By not selecting items based on practicality, they were wasting the taxpayers' money. In our walk-through of the facility we observed that the fitness balls that were intended to be on the tree were in fact on the floor and not being stored on the fitness ball tree.

The City has a fiduciary duty to ensure taxpayer dollars are protected and used only in the most prudent, efficient, and effective manner, guarding against waste and misappropriation. The items noted above show a lack of care over guardianship of the funds.

**Recommendation 08-08:**

We recommend that DGS and other City departments institute controls to ensure that funds are used in the most prudent manner possible. The choices made by project managers should be reviewed by their supervisors to ensure costs are being kept to a minimum and if using higher cost materials when similar lower cost materials are available, such costs should be justified in writing by the project manager and approved by their supervisor. When deciding on material to



be used for projects, in particular projects of a nature and type where the general public will not have access to or derive direct benefits from the aesthetics chosen, we recommend that the materials and designs selected be based on practicality and cost more than on design and aesthetics.

### **City Response:**

DGS serves as the subject matter expert in repairs and renovations for City facilities. In this capacity, DGS strives to make sure funds are used in the most prudent manner possible, balancing the wishes of client departments with budget realities and long term maintenance.

#### Terrazzo Wall

The audit incorrectly contends “the wall could have easily been painted at a cost of \$1.13/SF or \$578.56 ...” In fact, it was more cost effective to tile, not paint the wall. A tiled wall is more durable and requires less upkeep. A painted wall requires patch work (especially at the corners) and can require repainting several times during a year. Instead of \$578.56 the life cycle cost of the painted wall would be a minimum of \$10,000. In addition, in order to paint the wall, DGS would have to prohibit use of the workout room for at least a day. On the contrary, maintenance of a tiled wall would require scrubbing with soap and water a couple times a year at very little cost.

#### Drinking Fountains

Stainless steel drinking fountains are the City standard. Stainless steel drinking fountains are a better long term solution due to their durability, ease of maintenance, and in promoting a healthy and sanitary workplace. These units were also selected due to the fact that they replaced existing non-ADA stainless steel fountains. White enameled drinking fountains chip, crack and rust thereby needing replacement much sooner than stainless steel.

#### Chrome Fitness Ball Tree

DGS provided a ball tree that was functional efficient, and well-designed for the space provided.

### **IGO Response to City’s Response:**

In the City response, DGS indicates that it was more cost effective to tile the wall over the long run as opposed to painting it. In doing so, the City takes issue with the audit estimate for painting at \$1.13/SF, or \$578.56 for the entire wall. The estimate used by the IGO is based on actual costs for painting by DGS contractors in other City projects. In other words, the estimate comes from the City itself. Having secured such a rate in the recent past, it seems reasonable that the City could do so in the future. A life cycle cost of \$10,000 to maintain a 518 SF wall seems quite excessive and, if true, suggests a monumental maintenance problem for the vast number of other City buildings in which painted walls predominate.

We do not quarrel with the City’s characterization of the Chrome Fitness Ball Tree as functional, efficient, and well-designed for the space, rather, we take issue with its seeming extravagance given the \$1,314.62 price tag.

**Finding 08-09: Poor Controls Allowed Expenditures to be Paid that were Non-Eligible or Unauthorized Uses of TIF Funds**

As part of the TIF audit in addition to expenditure reviews of selected projects, we examined individual expenditures listed in the Annual Reports of the Central Loop and Central West TIF districts. We chose a judgmental<sup>13</sup> sample of expenditures perceived to be unusual in nature based on the supplier name, as well as a random sample of expenditures for the years 2006 and 2007.

We reviewed 21 vouchers issued during the years 2003 thru 2007 with supporting documentation that in our judgment appeared unusual. We determined that six of the 21 vouchers were non-eligible charges to the TIF fund and one was inappropriately charged to the Central Loop TIF.

The three vouchers detailed below, initiated by the DoIT and totaling \$6,230.58, were non-eligible expenditures:

Voucher Number	Supplier	Amount	Description
PV06070601279	W.G.N. Flag & Decorating Co.	\$ 449.50	U.S. Flags
PV06070600957	Systems Solutions, Inc.	\$ 899.00	HP Printers
PV06070600731	Xerox Corporation	\$4,882.08	Copier Lease

We contacted DoIT management to discuss why these vouchers were charged to the Central Loop TIF. They informed us that the department was originally budgeted TIF funds for a project and that the above expenditures were charged to the remaining funds from the budgeted TIF project in order to “exhaust the remaining funds” that were left over.

We also determined that voucher number PV08070800440 to Globetrotters Engineering Corp in the amount of \$14,282.37<sup>14</sup> for project development and management was inappropriately charged to the Central Loop since none of the projects listed were within the Central Loop TIF district. Through random expenditure testing we also discovered a voucher paid to Gibbons & Gibbons Ltd for appraisal services in the amount \$630.00<sup>15</sup> charged to the Central West TIF in error.

DCD was contacted regarding these charges, and we were informed that they were working with the DOF to pursue proper adjustments.

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<sup>13</sup> Judgmental sampling is discretionary; that is, the auditor bases the selection of a sample on knowledge or judgment about characteristics of the population.

<sup>14</sup> The DOF has removed the expenditure from the Central Loop TIF on September 9, 2009 charging it to the City of Chicago Corporate fund.

<sup>15</sup> The DOF has removed the expenditure from the Central West TIF on September 9, 2009 charging it to the City of Chicago Corporate fund.

**Recommendation 08-09:**

We recommend that the OBM provide instructions to departments to reinforce the fact that TIF funds earmarked for specific projects that are not fully expended on those projects per the budgeted amount, must be returned to the TIF fund, and that excess project funds can not be used for other purposes.

We also recommend that DCD institute additional reviews of expenditures being charged to TIF districts in order to reduce the possible occurrence of erroneous charges to the wrong TIF district.

**City Response:**

The City agrees with the recommendation and transferred the identified expenditures.

In addition, the Budget Office will provide written instructions to departments identifying allowable expenditures under the TIF Act, as well as the appropriate close-out procedures when projects are complete.

And as noted in finding 08-02, earlier this year, OBM, under the direction of the Chief Financial Officer, assumed responsibility for managing and monitoring all TIF funds and accounts. This important realignment of responsibility should greatly strengthen the oversight of TIF expenditures in all areas.

Finally, audits of TIF districts are performed annually. Per standard auditing practice for any government or private sector entities, the TIF audits utilize random sampling of transactions and therefore, do not examine each expenditure.

However, the Finance Department will perform additional expenditure reviews to determine expenditures meet the criteria of the TIF Act.

**Finding 08-10: Administrative Policies and Procedures for TIF Allocation of Salary and Overhead Costs are Non-Existent**

The 2007 TIF administrative allocation process is part of a cost allocation plan guided by federal OMB Circular A-87. This Circular establishes principles and standards for determining costs for federal awards carried out through grants, cost reimbursement contracts, and other agreements with State and local governments and federally-recognized Indian tribal governments (governmental units). While the TIF program is not required to follow A-87, the City has engaged Maximus Consulting to include TIF related administrative costs as part of their overall City allocation plan.

The Illinois General Assembly approved language in the TIF Act allowing Municipalities the ability to pay themselves for administrative costs. The language established in the Illinois TIF legislation is more restrictive than the OMB Circular A-87 in that Municipalities are prohibited from billing for administrative costs that would not have occurred if the TIF was not in place.<sup>16</sup>

Relying on the above provision in the TIF legislation and utilizing the methodology established by OMB Circular A-87, \$8,030,527 was charged to TIF districts and allocated back to the City of Chicago as reimbursement for employees participating in TIF related projects during 2007 and other related overhead. The TIF administrative allocation includes salaries, overhead and fringe benefits costs. The total \$8,030,527 allocated consists of \$4,633,309 related directly to salaries, \$1,766,770 for overhead and \$1,630,448 for fringe benefits.

We reviewed the salaries submitted by City departments for allocation comparing the amounts to the CHIPPS payroll as of 1/16/2007. We reviewed the percentages used to determine the amount of time each individual being allocated spends on TIF projects. We traced the percentages to records maintained by the departments along with their methodologies for determining how they arrived at the percentage of time for each person. Additional review steps were performed as follows: TIF fund allocations were traced from each TIF district fund account to the DOF allocation schedule for the year 2007 with no errors noted. TIF salary allocations were reconciled to the TIF district Annual Reports for the same period with no errors noted. Finally, a sample of employees was selected and interviewed to understand their involvement with TIF projects and to determine if their department requested them to keep track of and report their TIF related activities. These interviews helped us to obtain an understanding of the allocation percentages reported.

According to OBM and DOF the process works as follows: Various departments participating in the TIF allocation process submit a budget to OBM in the second half of the year. The budgeted amounts include the staff that worked on TIF projects, their individual percentage of time spent on TIF work, and their individual salary amounts budgeted for the year. OBM reviews this

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<sup>16</sup> (1.5) After July 1, 1999, annual administrative costs shall not include general overhead or administrative costs of the municipality that would still have been incurred by the municipality if the municipality had not designated a redevelopment project area or approved a redevelopment plan. Tax Increment Allocation Redevelopment Act, 65 ILCS 5/11-74.41.1

information for comparison to department salary budgets. OBM then forwards the departments' TIF employee participants list to the DOF. The DOF forwards the listing of TIF employees to Maximus, (an independent consulting company retained to prepare the City's yearly allocation for both TIF-related costs and federal and State grant allocations of staff working on TIF or grant related projects). Maximus is charged with making sure that City department cost allocations are not duplicated so that an individual's allocation is not greater than 100%. After the allocation has been completed by Maximus the information is then used by DOF to complete the journal entries necessary to allocate indirect department costs back to the TIF funds.

We obtained the 2007 allocation completed by Maximus and traced the amounts charged to overhead (\$1,766,770) back to the corresponding departments that contributed overhead to the TIF allocation. The components making up overhead were also reviewed. This included building and equipment depreciation, postage, Human Resources, Procurement Services, General Services, and Business Information Services overhead allocations.

Based upon our review and analysis, five potential findings and our recommendations have been provided. Findings are based on tests performed and interviews conducted with representatives from the DCD, DOF, DGS, Department of Law, City Treasurer, CDOT, and Maximus.

**A. \$130,246 was improperly allocated from TIF money to the corporate fund to pay for a vacant position and to pay employees who started or terminated in mid-year.**

Each year City departments that have employees whose job duties relate to TIF activities are allowed to have their salaries reimbursed from TIF district funds based on their percentage of job activity that relates to TIF performed functions. The State of Illinois TIF Act states "annual administrative costs shall not include general overhead or administrative costs of the municipality that would still have been incurred by the municipality if the municipality had not designated a redevelopment project area or approved a redevelopment plan." The legislation allows administrative cost reimbursement for salaries so long as the individual is participating in TIF-related work and if the TIF work did not exist the employee would not be required. These allocations are to be based on the employee's percentage of time spent on TIF projects multiplied against their yearly budgeted salary.

DCD submitted a vacant position for TIF payroll reimbursement to OBM in the amount of \$67,656 or the equivalent of 100% TIF work related participation. The funding of a vacant position confirms there is a lack of controls within the review process of OBM and DOF where the actual allocation is completed resulting in TIF funds being transferred out of the TIF districts improperly and in violation of the TIF Act. No person was active in this position during the entire year and therefore this submission resulted in the City improperly transferring funds from the TIF fund to the City Corporate fund. Once the money has been removed from the TIF fund and transferred to the City Corporate fund the City is no longer bound by TIF legislation restricting fund use.

We also noted four instances in our review of the 2007 TIF salary allocation where an individual's salary had been over-allocated based on 12 months participation in TIF activities, when in fact they were hired or terminated with partial year participation in TIF projects. We

determined two individuals were hired in May 2007 and one individual in February 2007 resulting in seven months and ten months participation, respectively. One individual terminated mid-year (May, 2007). All four individuals were allocated from TIF funds for the entire year. Allocating TIF salary for the entire 12 month period for these employees resulted in overstating the TIF salary allocation.

The lack of written policies and procedures for departments to follow in submitting a list of individuals who belong in the TIF allocation but worked for less than a full year caused departments to over-allocate funds based on full year of participation instead of the actual percentage of time participating in the TIF activity. This over-allocation resulted in an improper transfer of \$62,590<sup>17</sup> by the TIF funds to the City's Corporate Fund where the monies can be used for any purpose.

**B. The date used in determining the salary to be allocated to TIF districts was inconsistently applied by the City departments participating in the TIF payroll allocation process.**

Good business practices would dictate that as part of the TIF salary allocation process the departments use a standard payroll date to establish salary used for employees whose duties include TIF activity. The City of Chicago pays on a bi-monthly system therefore; there are 24 payroll reporting periods. Within the year individuals may receive increases which change their salary or pay going forward. Since the employee's salary may increase at various times during the year it is essential to establish a firm payroll reporting date to be used in the calculation for TIF payroll allocation. We were unable to find documented policies indicating what payroll period should be used in determining the date used for the TIF payroll allocation. Departments we reviewed appeared to have used different dates for reporting the employees' salaries to OBM. These inconsistencies indicate a breakdown in the controls for a main component of the salary allocation process establishing the amount of salary to be allocated to the TIF districts for employee's participating in TIF activities. This, in turn, may result in overcharges/undercharges to the TIF funds by overstating/understating salary amounts being paid in comparison to approved salary budgets. This becomes an issue when departments do not use the same payroll reporting period each year for the allocation.

There is no written policy establishing the date City of Chicago Departments participating in TIF salary allocation must use in determining the amount of salary for individual employees whose salary is being allocated to the TIF districts. Lacking a definite payroll reporting date has resulted in departments using different payroll reporting periods to define the individual's pay for the TIF allocation. We found that out of the 125 employees whose salary is being allocated to the TIF districts, 37 employees' salaries were based on dates of pay other than the first payroll reporting period in 2007.

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<sup>17</sup> It should be noted that the over-allocation of salaries resulting in the \$62,590 could be offset by employees filling vacant positions that existed at the beginning of the year. The time required to verify if this is the case is not worth pursuing for the dollar amount involved. It is more important to establish procedures that do not allow for funding positions at full year salary amounts if individuals start or quit during the year.

The amount of each employee's salary used for determining the TIF payroll allocation is dependent on the payroll reporting date. An employee's salary on the first payroll period of the year may not be that employee's compensation every month of the remaining year. We reviewed individual salary amounts used to compute TIF payroll allocation as of the first payroll reporting period in 2007 (1/16/2007). During this review, we noted that 37 instances or 29.6% of the allocated salary amounts used to calculate the percentage of TIF reimbursement did not match actual salary amounts reported in the City of Chicago payroll system on 1/16/2007. We also found instances where individuals received increases during the year; however their salary used for determining the allocation was not adjusted for the increase demonstrating the lack of consistency from not having a policy establishing firm reporting dates.

**C. Minimal documentation to support the percentage used in allocating employee time spent on TIF projects was retained.**

We noted 90 out of 125 (72%) employees being paid from TIF funds were found not to have sufficient documentation to support the percentage of time they spent on TIF related activities in their jobs. Interviews of selected employees paid from TIF funds disclosed discrepancies between the percentages claimed by the respective departments and the individual's actual job duties. Interviews also disclosed that employees, in most cases, were not required to track their time or report their time on TIF duties in any way. The percentage of time individuals spend on TIF related projects is one of the determining factors used to calculate TIF salary allocations from TIF district funds. Departments submitting salary allocations must be able to substantiate and support each employee's percentage of time spent on TIF projects in order to comply with acceptable cost allocation methodologies, such as OMB Circular A-87.

In our review we were unable to find any current documentation providing the departments participating in TIF allocation with guidance on how to track individual employees' percentage of time spent on TIF activity other than a memo from John Harris, Director of OBM in May 2004, to Denise Casalino, then Commissioner DPD, discussing specific positions that existed within the DOH in 2004.

By not providing departments participating in the TIF allocation process with guidelines or an approved methodology, the departments are left to determine their own way of establishing the percentage used in the calculation which may or may not be accurate or valid. In not maintaining adequate documentation supporting the employee's time, the percentage used becomes nothing more than a guess or estimate, which, by definition, is not actual and can lead to abuse by over-allocating TIF district funds. Alternatively, if departments underestimate the percentages to apply to employees' allocated TIF work, the City would not be able to recoup funds to which it is entitled.

**D. A listing of City department employees participating in TIF activities obtained from OBM and the DOF did not match employee lists submitted independently by the departments participating in TIF allocation.**

We found 15 instances in which City departments submitted individuals for inclusion in the allocation process that were not on the list used for the actual allocation. Additionally, we found that the actual allocation included nine employees that were not on the lists submitted by the City

departments. We reviewed the lists obtained from each department comparing them to the actual employees that were allocated from TIF district funds. We determined that eleven employees on the list obtained from MOWD were not used in the actual allocation and four employees DOH submitted to OBM and the DOF for inclusion were not used for the TIF payroll allocation. We also determined that for DOH, nine employees were included in the actual TIF payroll allocation that were not listed on the payroll allocation sheets sent to us from DOH. These discrepancies could not be explained by the MOWD, DOH, OBM, or the DOF.

These differences in documents demonstrate a lack of coordination between OBM, DOF, and the departments submitting names of employees to be paid from TIF funds. In order to allocate expenses properly and in accordance with acceptable cost allocation methodologies, individual employees submitted to OBM and DOF for inclusion in TIF salary allocation must be based on the employees' documented time spent on TIF related projects.

Additionally, because there is no documentation indicating department Commissioners or their designee reviewed the final list of employees being submitted for allocation, there is a lack of accountability over the process. This lack of Commissioner or designee review and approval may result in employees being added or substituted that may not actually be participating in TIF activities for the purpose of reducing employee budgeted payroll costs.

#### **Recommendation 08-10:**

We recommend that written policies and procedures be established and provided to the departments that participate in the TIF Administrative Allocation process that:

- a) restrict departments from submitting vacant or unfilled positions for TIF payroll allocation. These procedures should require sign-off by the department Commissioner or designee indicating they have reviewed the list of employees being submitted for allocation and certify to its accuracy. The certification should be maintained by DOF for verification and review. A policy should also be established to address when and how departments report new hires and terminations to OBM. DOF should review and compare the individual employee names, hire, or termination date submitted by the participating departments against independent payroll data maintained by Human Resources, to ensure they are properly allocated in the correct periods.
- b) require uniform payroll reporting dates be established that incorporate salary increases anticipated per approved budgets and or union agreements. Specific guidelines should be written into the policy providing the department's guidance for notification to OBM of when and how to provide the required documentation necessary for reductions in salary and overhead allocation as a result of furlough days and or non-paid holidays
- c) include the methodology to be used and the documentation required to be maintained by departments in determining how employees' percentage of time participating in TIF related activities are determined.

We further recommend that the \$67,656 allocated from TIF funds to the Corporate fund to pay for the DCD vacant position be returned to the TIF districts.



**City Response:**

First – the vacant DCD position included in the allocation was a clerical error, as eleven of the twelve vacant positions provided to the Department of Finance were properly excluded from the allocation.

The Office of Budget and Management will ensure these positions are excluded from the analysis before it is sent to be processed by the Department of Finance.

Also, the Office of Budget and Management will, going forward, include the employee identification number on the allocation worksheet, and the Department of Finance will use that information to pull the employee's gross salary information directly from the payroll system. This will eliminate any possible variances as a result of changes in salaries, furlough days, etc.

As part of the City's cost allocation methodology for OMB A-87 several methods are used based on the departments function such as time performed, transactions processed, etc. Therefore, OBM and Department of Finance felt the departments participating in the allocation would have the best knowledge to determine the methodology most appropriate for that department.

The Department of Finance and Office of Budget and Management will assist the Office of Compliance to develop policies and procedures to ensure the percentage of time that employees spend on TIF work is appropriately documented, and that department heads review and approve the employees and the percentage of their work that is allocated to TIF.

**Finding 08-11: WBE Credit Related to Vendor Subcontracts was Miscalculated and Based on Misrepresentation**

As part of our review we looked at Compliance Assessment Memorandums for the contractors used to remodel the Police Academy. For this remodel there were two contractors, Paul Borg and Old Veterans Construction. As part of compliance assessment, DPS performs a review of Minority Business Enterprise (MBE) and Women Business Enterprise (WBE) commitments. In the contracts the City of Chicago goal for MBE is 24% and for WBE 4%

In our review of the goals achieved by Old Veterans under sub job order JV5-085D for MBE, DPS calculated their dollar attainment at \$19,398.38 or 10.7% and WBE at \$161,080.00 or 84.8% of the job order total which was based on Old Veterans sub-contracting to Q.C. Enterprises, Inc., a certified WBE. Q.C. Enterprises, Inc was credited by DPS for the full \$161,080.00. Based on our review however, we determined that Q.C. Enterprises, Inc. subcontracted to two other companies Menconi Terrazzo and Tile for \$19,000.00 of the \$161,080.00 and to Chicago Floor Systems for \$109,580.00 of the \$161,080.00. Neither of these companies was listed by DPS as a certified WBE. We also noted on the Contractor's Affidavit that Q.C. Enterprises, Inc. provided materials for this project in the amount of \$32,500.00 which is the amount that DPS should have used to calculate WBE attainment of 18% not 84.8%.

We found that DPS calculated WBE attainment for another sub-job order JV5-085F in the same manner and did not deduct the amounts Q.C. Enterprises, Inc. sub-contracted to other companies. In the case of JV5-085F, Q.C. Enterprises provided labor totaling \$78,529.00 and not \$95,129.00 for which they were being originally credited. The correct percentage attainment should have been based on the \$78,529.00 and not the \$95,129.00. The difference of \$16,600 was comprised of services provided by Menconi Terrazzo and Tile totaling \$10,300.00 and Kraftex Floor Corporation totaling \$6,300.00; neither of these companies were WBE certified companies.

We met with DPS to discuss the inaccurate calculation of the WBE credit. DPS indicated the reason for the inaccuracy in the calculation may have been caused because the subcontractor, Q.C. Enterprise later decided to sub-contract out some of the work and failed to correct the initial paperwork. Another reason provided was that the general contractor (Old Veterans) decided to assign another sub-contractor some of the work again after the initial paper work was filed with DPS. We can not determine by reviewing the documents if Old Veterans told Q.C. Enterprise that additional suppliers were going to be used and therefore Q.C Enterprise was also misled initially when they submitted the original documents used by DPS. If Old Veterans directed Q.C. Enterprises, Inc to use other suppliers, Old Veterans had an obligation to inform both DPS and DGS of the change. Old Veterans filed disclosure documents indicating that Q.C. Enterprise was going to be the subcontractor for the entire \$161,080. The Schedule C document filed by Q.C. Enterprises also indicates they were going to be the subcontractor for the entire \$161,080. The affidavit or lien waiver filed by Old Veterans indicates Q.C Enterprise as the subcontractor. The affidavit or lien waiver filed by Q.C. Enterprises however, indicates that they were subcontracting out most of the work.

The documents that DPS received from the contractor are misleading, however both Old Veterans and DGS knew that Q.C. Enterprise was subcontracting out the work since both were at the job site continually and as such had an obligation to inform DPS. Therefore, due to lack of clear policies and procedures in place, both DGS and the contractor, Old Veterans, played a role in allowing the WBE credit to be miscalculated by DPS.

**Recommendation 08-11:**

We recommend that DPS recalculate the WBE credit awarded to Old Veterans affected by the misrepresentation of the documents. DPS should also meet with Old Veterans and Q.C. Enterprise to determine why the documentation submitted to the City does not accurately reflect the true nature of the relationship Q.C. Enterprise purported to have as a sole subcontractor. DPS should review Q.C. Enterprise documentation submitted for other projects to determine if this is a recurring problem or an isolated one and take appropriate action if the documentation indicates it is a recurring problem.

We also recommend that DPS remind all general contractors that failure to notify DPS and user departments of accurate subcontracting is a violation of City policy and procedure, and Chapter 2-92-730 of the Municipal Code of the City of Chicago (Contract performance procedures), that may result in loss of contracting ability. Additionally, user departments are responsible for providing DPS with accurate documentation. Since the user department Project Manager knows what subcontractors were used on the job site, procedures should be established mandating the user department Project Manager to review all subcontractor lien waivers for accuracy and then send to DPS the verified lien waivers or submit to DPS accurate lien waivers reflecting all subcontracting by subcontractors if the lien waiver received from the general contractor does not accurately reflect all subcontracting. DPS should establish new procedures that require comparison of contractor submitted lien waivers to user department verified lien waivers prior to completing assessment letters.

**City Response:**

DPS, working with OCX has recalculated the WBE credit for the 2 suborders at issue. DPS determined that the accurate number for the WBE percentage is significantly less than reported and should have been 10.8% and 22%, both of which exceeds the commitment for the suborders. DPS has scheduled a meeting with Old Veterans and Q.C. Enterprise to determine why the documentation submitted to the City does not reflect the true nature of the relationship Q.C. Enterprise purported to have as a sole contractor and issued a revised M/WBE assessment letter. DPS will also work with OCX to conduct an audit of Q.C. Enterprise on any other projects.

At the close-out of suborders, the JOC contractors are required to submit lien waivers, including those of lower tier subcontractors. The closeout process is intended to catch these situations where a vendor has not accurately reflected the MBE/WBE participation in their original Schedule C and not updated their compliance plan if any changes had occurred.

DPS will include these issues in the JOC refresher course for all JOC contractors to remind them that failure to notify DPS and user departments of accurate subcontracting is a violation of their contract, municipal ordinance, and City policy and procedure that may result in loss of contracting ability.

**NON-COMPLIANCE:**

**Finding 08-12: Expenditures Submitted to the City of Chicago by the PBC for Reimbursement are Not being Reviewed for Compliance with the TIF Act**

During the years 2003 thru 2007 (the selected audit review period) the Central Loop TIF distributed \$94,856,508.00 to the PBC for various projects which it managed. In our review, as described below, we determined that expenditures by the PBC paid from TIF funds were not being reviewed for compliance with the TIF Act by either the PBC or the City.

A random judgmental sample was selected from the 2005 TIF fund Expenditure Report for all transactions involving the PBC. The vouchers reviewed were as follows:

PV Number	Payee	Amount	Date
PV05050560170	PBC	\$13,400,000.00	11/18/2005
PV05050560140	PBC	\$ 3,809,977.00	10/07/2005
PV0505050066	PBC	\$ 118,013.11	05/02/2005
PV0505050066	PBC	\$ 160,230.71	05/02/2005

We contacted the PBC requesting detailed invoice documentation supporting the above TIF expenditure reimbursements to the PBC. Upon our review of these documents at the PBC we determined that the \$13,400,000 payment was the result of a court ordered settlement with various suppliers and determined that this was not valid to pursue for further documentation other than obtaining a copy of the settlement agreement and verifying the fund transfer.

We requested documentation from the PBC supporting the reimbursements for the other three charges and were informed that expenditure documentation would not tie into the dollar amount reimbursed from the City to the PBC because costs are not reimbursed based on actual expenditure detail that totals to individual invoices or documentation. Project funding payments to the PBC are based on estimated costs submitted by the PBC to the City and later reconciled to actual expenditures by line item or category of expenditure less prior payments.

In reviewing this documentation we could not determine that the payments matched to any specific charges (invoices) and therefore could not verify that these are legitimate TIF expenditures as allowed by the TIF Act.

The Director of Finance at the PBC was able to provide the auditors with the Expanded General Ledger Detail Report for the two projects associated with the three payments. The two projects were the Harold Washington College Rehabilitation and Millennium Park Project F-2. The Harold Washington College Rehabilitation consisted of funding from the Central Loop TIF

district of \$38,626,542.99 and expenditures which totaled \$37,433,138.57, and the Millennium Park Project F-2 consisted of funding from the Central Loop TIF totaling \$26,257,346.53 and expenditures of \$26,248,254.06.

Using the Expanded General Ledger Detail we selected various line item expenditures to review. Since we were unable to verify expenditures based on the City's reimbursement, we reviewed the expenditures in totality for reasonableness and compliance with the TIF Act.

For the Harold Washington College project we selected 39 invoices out of 305 or 13% totaling \$9,491,320 or 25% of the total dollars spent. For the Millennium Park project F-2 we selected 30 out of 100 invoices or 30% totaling \$3,943,575 representing 15% of the dollars spent.

In our review of payments to the PBC from TIF funds we found that expenditures submitted to OBM for payment are not verified for compliance with the TIF Act. The process works as follows: 1) The PBC submits a "Request for Payment" to OBM. The request for payment is based on estimated project disbursements by the PBC through a specific date, plus the difference between funding from the City to the PBC less PBC disbursements to date. 2) While the PBC does include a "Cost by Activity Report" that provides a cumulative cost by expense category to OBM, the PBC does not submit a detailed invoice of expenditures by category for OBM to review.

Since OBM does not review detailed invoices it is unable to certify that the expenditures being submitted by the PBC are TIF eligible per the Act as indicated in the payment of \$329,000 to DCA in finding # 08-09 and the payments of \$11,486.23 and \$73,395.93 to a jobs training program called the Skill Builders Program that is also not an eligible TIF expenditure under the Act. (See Finding # 08-11).

These non-eligible expenditures occurred because neither the PBC nor the City OBM was verifying that expenditures from TIF Funds were in accordance with the TIF Act.

Good internal controls over the expenditure process would require that the PBC and the City OBM both review detailed expenditures submitted for reimbursement prior to payment using TIF funds to ensure only TIF eligible expenditures are paid from TIF funds.

#### **Recommendation 08-12:**

We recommend that in order for the City to ensure that PBC requested expenditures are TIF eligible, the City establish an expenditure review procedure by employees from OBM familiar with the TIF Act and they have sufficient detail to certify compliance; sufficient detail being original invoices along with documentation supporting receipt of goods. Additionally, the City should cease any further TIF funded payments to the PBC until the proper review process is established.

**City Response:**

As noted in the response to recommendation 08-09, audits of TIF districts are performed annually. Per standard auditing practice for any government or private sector entities, the TIF audits utilize random sampling of transactions and therefore, do not examine each expenditure.

Also as noted in that same response, the Finance Department will institute additional expenditure reviews to determine if expenditures met the criteria of the TIF Act.

However, even as the Department of Finance works quickly to establish the additional expenditure review, it is unreasonable to suggest that the City cease any further TIF payment to the PBC at time, and the City strongly disagrees with that recommendation.

As noted in the response to finding 08-01, the Public Building Commission (PBC) acts as the City's general contractor on various City projects. As such, it relies on funding from the City to initiate and complete these projects as it does not have a separate revenue source. Therefore, the City must front funds based on an estimate from the PBC of their cash needs for a period of sixty days.

And finally, as noted in the response to finding 08-06, the City strongly disagrees that liquidated damage payments made by the PBC to the Skill Builders Program are ineligible TIF expenditures.

When the contractor completes the project, they are entitled to payment of the contract sum. However, the City disagrees with the assertion that liquidated damages collected must be returned to the TIF. As a legal matter, when a contractor completes the project, they are entitled to payment of the contract sum (the source of which could be TIF funds); therefore, the funds paid or payable under the contract become those of the contractor.

Liquidated damages, therefore, are not considered TIF funds governed by the TIF Act.

And in fact, the City's resident hiring ordinance (Section 2-92-330 of the Municipal Code of Chicago) requires that residency damages are used to establish worker training programs.

It is also appropriate to note that under the City's city resident hiring ordinance requirements. Section 2-29-330 of the Municipal Code of Chicago, subsection (e) thereof provides that "(e) The monetary damages stipulated in subsection (b) hereof shall be used for establishing a worker training program." The Skill Builders Program is such a program.

**IGO Response to City Response:**

Referring to the City's position regarding liquidated damages we again reference our response in Finding 08-03.

**Finding 08-13: Calculations Used for Determining Income Eligibility to Purchase TIF Subsidized Housing were Inappropriate**

The City Council, pursuant to an ordinance adopted by the City Council on April 9, 2003 and published at pages 105808 through 105832 in the Journal of the Proceedings on such date, which ordinance approved a Public Housing Transformation TIF program (the “Program Ordinance”); authorizing the use of TIF money from the Central West TIF district for development costs of condominiums to be built for the Horner/Westhaven Park Phase IIA1 Low-Rise Transformation Project Redevelopment Agreement known as WHP Homes.

The Developer was to be provided up to \$2,350,000 in TIF assistance to build 60 residential condominiums of which 12 were to be designated as income-qualified for sale units.

The RDA as approved by the City Council defines Qualified Household as:

“a single person, family or unrelated persons living together whose adjusted income is not more than eighty percent (80%) of the Chicago area median income, adjusted for family size, as such adjusted income and Chicago area median income are determined from time to time by the United States Department of Housing and Urban Development for purposes of Section 8 of the United States Housing Act of 1937. **As of the Closing Date**, such income limitations are as follows: (emphasis added)

# of Persons In Household	100% of Chicago Area Median Income
1	\$52,800
2	\$60,300
3	\$67,900
4	\$75,400
5	\$81,400
6	\$87,500”

As part of our review we requested the documentation and methodology used by the DOH, now a part of the DCD for income determination of selected individuals that acquired condominium units under the Qualified Household provision.

When reviewing documentation from the DCD on three selected qualified applications, we found that two of the three had income determinations based on the date they signed an agreement to purchase the condominium units, which was in 2003. We determined that these individuals had closing dates in 2006 and 2007 which per the Qualified Household definition should have been the date used for income determination.

Additionally, a memo dated August 1, 2005, provided to us by DCD from a DOH Deputy Commissioner who had the responsibility for qualifying incomes of potential purchasers, stated that the developer of WHP Homes made an error in determining eligibility and allowed contracts to be signed back in 2003 and 2004 without prior approval from DOH. The letter further indicates that DOH will change the income determination date to 2003 instead of the closing date in order to avoid potential problems.

We interviewed the former DOH Deputy Commissioner, who now works in a different capacity at DCD, to determine if the City of Chicago Law department was consulted since the change was not consistent with the City Council Ordinance. He indicated that the then Commissioner of DOH approved of the change but no documentation could be provided on whether the Law department was consulted.

He further explained that at a meeting with the developer prior to issuance of the memo, the developer was informed that he went beyond the authority allowed, by approving individuals and accepting signed agreements for qualified low income housing purchase without the DOH first approving. DOH made the decision to accept the 2003 income determination to avoid any bad publicity or potential law suits.

We were further informed that since this occurred, policies and procedures have changed within DCD that eliminates this problem from occurring. We reviewed the current procedures in place and have verified that they are sufficient if followed.

**Recommendation 08-13:**

We recommend that DCD continue to follow the current procedures established for reviewing and qualifying low income housing purchasers.

**City Response:**

As recommended, relevant policies and procedures have been amended to address this issue, and those procedures remain in place.



**TRANSPARENCY:****Finding 08-14: The Decision to Port Money is Determined by Non-Elected City Employees called the “TIF Task Force” with no Disclosure to Taxpayers or the City Council until Annual Reports are Filed**

Current practices for porting of TIF funds from one district to another do not allow for the residents of those TIF districts or the City Council to know where and how these tax dollars are being spent. Additionally, the decision-making process for porting funds is controlled by a small group of City employees with no formal policies and procedures in place and no documentation of decision criteria.

The Illinois TIF Act 65 ILCS 5/11-74.4.41 (q) defines porting as: [the ability to] “Utilize revenues, other than State sales tax increment revenues, received under this Act from one redevelopment project area for eligible costs in another redevelopment project area that is:

- (iv) contiguous to the redevelopment project area from which the revenues are received.
- (v) separated only by a public right of way from the redevelopment project area from which the revenues are received; or
- (vi) separated only by forest preserve property from the redevelopment project area from which the revenues are received if the closest boundaries of the redevelopment project areas that are separated by the forest preserve property are less than one mile apart.”

The City uses porting as a method to fund projects within contiguous TIF districts that do not have sufficient available money for the project. DCD management indicated that this may occur because the receiving TIF district is new and property tax revenue has not built up to sufficient levels, or prior projects have depleted the available funds for new projects determined to be urgent in nature. During the years 1997 through 2007 \$138,384,232 was ported between TIF districts.

Based on discussions with DCD and OBM, the decision on when money should be ported for infrastructure projects is made by a group consisting of the Director of Capital Projects, OBM as Chairperson, DCD deputies, and various representatives from the departments receiving TIF funds. This group is called the TIF Task Force. This Task Force is responsible for reviewing requests from City departments, aldermen, and the Mayor’s Office for use of TIF money to finance infrastructure projects. It is the responsibility of this Task Force to decide if the projects should be funded with TIF money. Other type project funding decisions such as IGAs and RDAs are principally decided by DCD. In our discussions with DCD regarding the current process we were told that the Mayor’s Office, aldermen in the TIF districts where funds are being ported from and to, and other City departments’ management may at times be involved in the discussions but the ultimate decision to port funds is made by DCD.

No one involved in the process maintains meeting minutes documenting participants and criteria for porting determinations. There exists no current policy or procedure requiring the generation

and retention of such information. No records are kept documenting the individuals involved in the approving of specific porting actions, other than a memo sent from the DCD to the DOF requesting the funds transfer. There is no list of City employees authorized to approve porting, maintained at either DCD or the DOF.

Best business and government practices and guidance suggest that minutes be kept and made public to improve transparency and ensure that porting of funds occur only as a result of thorough discussion and analysis of need and pursuant to authorized channels and protocols for approval.

When decisions to move money from one TIF district to another are made without documentation and without public scrutiny, the citizens who contribute real estate tax dollars to the TIF district from which the money is being removed are deprived of their right to know the reasons and responsible parties for the diversion of their tax dollars. Such actions reduce the funds available for improvement projects within the originating TIF district and thereby potentially adversely impact the direct benefit of the citizens and businesses within that district for which the originating TIF district was established. We believe the existing decision process, which does not get documented through maintenance of detailed meeting minutes, perpetuates the notion of a secret process susceptible to undue and improper influences.

The lack of written documentation of participants and criteria used in the decision-making process significantly reduces transparency related to porting funds. Taxpayers are entitled to a clear understanding of the reasons for the utilization of their TIF district money in another taxing district. Additionally, the absence of a formal, published listing of individuals authorized to port funds increases the risk that unauthorized individuals may initiate transfers of TIF money from one district to another for budgetary or other reasons.

#### **Recommendation 08-14:**

We recommend that in order to reduce the appearance of undue influence and increase transparency in the porting decision process, TIF Task Force meeting minutes be retained by DCD indicating who was involved and the criteria used in the decision-making process. Additionally, DCD should establish a formal authorization list, to be retained by DCD and the DOF. This list should be updated on a yearly basis, and when authorized employees leave or job duties change, indicating who has the authority to approve porting and what the dollar level of that authority is, as higher dollar levels may require dual signatures or higher level management approval. We also recommend that porting decisions and meeting minutes be disclosed to the public on the DCD website, on a timely basis so that taxpayers know where their tax dollars are being spent. Publishing the minutes online would also provide timely disclosure to the City Council.

#### **City Response:**

First and foremost, porting TIF funds is a legal and allowable process under the IL TIF statute, and it is most often used to spark redevelopment in areas where new TIF districts are being

established. And the City only ports funds when needed and always for uses allowable under the state TIF statute.

Most commonly, uncommitted funds in a mature TIF are transferred to a new TIF to "jump-start" a project, thus accelerating the new TIF's ability to generate increment. The TIF will thus be more productive and efficient over its 23-year life. Otherwise, it may take several years for a new TIF to generate sufficient increment to support projects.

Because funds can only be ported to adjacent TIFs, residents in the original TIF boundary will often benefit from investments made to an adjacent TIF, as the items funded through porting serve an area that extends well beyond a TIF's boundaries. This is especially true of new schools and parks, but also commercial and industrial development that generates and preserves jobs. And in this way, porting helps both new and older TIFs by spreading economic activity over a larger community area.

Regarding transparency – TIF porting decisions are typically in the public domain well before approval, particularly when they are approved by City Council as part of a development agreement or bond authorization – this is true for the vast majority of TIF dollars that are ported.

These transfers of funds are also documented in the TIF annual reports that are posted on the City's website. When porting occurs, it is reported as a "transfer in" or "transfer out" of a TIF, depending on whether funds were moved into or out of a TIF.

TIF porting is also posted online in the new TIF Projection Report, which is updated on a quarterly basis.

And to enhance transparency even further, the City will agree to not consider porting any funds that have not already been previously posted on the TIF Projection Report.

### **IGO Response to City Response:**

During the ten year period 1997 through 2007, \$138,384,232 was ported between TIF districts, much of this money being used to renovate and build schools. This audit does not draw any judgment on the use of TIF money for such purpose. However, we note that when money is ported from one TIF district to another for the purpose of renovating and building schools, the school benefiting may not be within an area that allows children from the porting TIF district to attend. Additionally, the issue of what schools benefit and why is not transparent to the taxpayers of the porting TIF district.

We fully recognize the process of porting is legal, but this should not relieve the City's responsibility to have candid and open discussion with TIF district residents on the use of their tax dollars. Nor should it relieve the City of proper documentation and record keeping that is readily accessible and transparent to the public.

**INTERNAL CONTROL:****Finding 08-15: Material Ordered Directly by DGS In-House Trades was not Properly Verified as Received Resulting in the Potential for Theft**

Materials were both ordered and received by in-house trades without verification by the DGS project manager that all items ordered by the trades were received and used on the specific project to which they were charged.

The remodel of the Police Academy was completed by outside contractors ordering materials and services using the JOC system and City in-house trades such as carpenters and electricians from DGS performing specific work and ordering materials thru DPS.

In our examination of the expenditures associated with the remodel, we reviewed 28 invoices totaling \$63,932.82 from five different suppliers (contracted via the DPS procurement process) for tile, grout, paint, wood, valves, doors, nuts, bolts and door hardware that were purchased directly by the in-house trades who report to the Deputy Commissioner DGS Bureau of Trades and Engineering Management. The materials ordered by DGS in-house trades were shipped to either the City of Chicago Pershing or Throop Street facilities because the job site did not have a secure location for storage of materials or because specific prep work was required prior to installation at the Police Academy that was more efficiently performed at the Pershing or Throop facilities.

In our discussions with a DGS project manager we were told that the material is received and verified by the receiver (an in-house trades employee) at these locations. This was later confirmed by the Deputy Commissioner of The Bureau of Trades and Engineering DGS. Our review of the supporting documents indicated that the materials were being verified by the DGS in-house trades as received. It should be noted that the person receiving may also sometimes be the person that placed the order. We also inquired how the DGS project managers assured themselves that the materials received at the warehouses were actually used at the Police Academy job site. We were informed by the DGS project manager that he relied on "trust". No formal documents were maintained verifying receipt at the Police Academy. We were further informed by the project manager that sometimes materials are used on other job sites. Since materials are being received at locations other than job sites, and since verification of materials ordered for a job site against the materials actually used on the job is not performed, the potential for theft of these materials is increased.

Good internal control procedures would require a separation of duties between ordering and receiving functions, and that the responsible project manager have a process to verify that the items ordered and paid for out of project budget are used only on that project.

**Recommendation 08-15:**

We recommend procedures be put in place to ensure that there are different individuals responsible for ordering and receiving of goods and that the responsible project manager have a process to verify that the items ordered and paid for out of the project budget are used only on

that project. Project managers need to be accountable for making sure materials ordered for use on projects that are assigned to them are actually used at that job site and fully accounted for. Since the project manager is approving the expenditures of materials purchased through DPS by in-house trades, the project manager should be required to sign off on all invoices indicating verification of materials received at the job site.

**City Response:**

The City agrees with recommendation, and DGS plans to review, and strengthen its inventory controls around the receipt and issuance of goods/materials related to internal construction projects.