CITY OF SAN ANTONIO

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September 25, 2020

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SUBJECT: Audit Report of Neighborhood & Housing Services Mid-Town TIRZ

Mayor and Council Members:

We are pleased to send you the final report of the Neighborhood & Housing Services Mid-Town Tax Reinvestment Zone. This audit began in December 2019 and concluded with an exit meeting with department management in July 2020. Management's verbatim response is included in Appendix C of the report. Neighborhood & Housing Services Department management and staff should be commended for their cooperation and assistance during this audit.

The Office of the City Auditor is available to discuss this report with you individually at your convenience.

Respectfully Submitted,

Buddy Vargas for Kevin W. Barthold

Kevin W. Barthold, CPA, CIA, CISA
City Auditor
City of San Antonio

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CITY OF SAN ANTONIO

OFFICE OF THE CITY AUDITOR

Audit of Neighborhood & Housing Services Department

Mid-Town Tax Increment Reinvestment Zone (TIRZ)

Project No. AU20-023

September 25, 2020

Kevin W. Barthold, CPA, CIA, CISA
City Auditor

Executive Summary

As part of our annual Audit Plan approved by City Council, we conducted an audit of the Neighborhood & Housing Services Department (NHSD), specifically the Mid-Town TIRZ. The audit objectives, conclusions, and recommendations follow:

Determine if the Mid-Town TIRZ is operating in compliance with established guidelines.

The Mid-Town TIRZ is operating in compliance with established guidelines. NHSD has adequate administrative processes in place. Controls over fee collection are adequate and fee collection is accurate. In addition, reporting of Mid-Town TIRZ status to the State of Texas is accurate and timely. Further, controls over approvals, tax reimbursements, and compliance for Center City Housing Incentive Policy (CCHIP) projects are adequate. Finally, the Finance Plan is up to date and accurately reported. However, we noted improvements that could be made to Mid-Town TIRZ administration.

We recommend that the Neighborhood & Housing Services Department:

- Ensure developers submit and staff receive all required support documentation prior to reviewing applications and document any exceptions
- Review and streamline the Contract Progress Payment Request approval process
- Work with the City Attorney's Office to clarify the effective date of future agreements
- Establish a compliance monitoring program for TIRZ Projects.

NHSD Management agreed with the audit findings and has developed positive action plans to address them. Management's verbatim response is in Appendix C on page 10.

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Background

The City of San Antonio is dedicated to the revitalization of inner-city neighborhoods and commercial districts by using a tiered system of incentives, one of which is Tax Increment Financing (TIF). The TIF program was established in 1998 and helps support development projects intended to promote economic stimulus to surrounding areas of a Tax Increment Reinvestment Zone (TIRZ). TIF can be used to assist in financing needed public improvements and enhancing infrastructure. Taxing entities that collect taxes against property within a TIRZ have an opportunity to contribute these future tax revenues to a TIRZ fund to reimburse the costs of public improvements.

The TIRZ can reimburse costs associated with public improvements that benefit the zone as outlined in Texas Tax Code Chapter 311. Some of reimbursable costs include but are not limited to:

- The demolition of a private or public building
- Affordable housing in and outside of the zone
- The preservation of the façade of a private or public building
- Remediation of conditions that contaminate public or private land or buildings
- Construction of a road, sidewalk, or other public infrastructure in or out of the zone

The City of San Antonio established the Mid-Town TIRZ in December 2008 which falls under the TIF guidelines of that same year. In 2012, the Mid-Town TIRZ absorbed the River North TIRZ. Subsequently, City Council extended the term by three additional years until September 2031. For a map of the current Mid-Town TIRZ boundaries, see Figure 1 in Appendix A.

The TIF Program is managed by the Neighborhood and Housing Services Department (NHSD), specifically the TIF Division. The TIF Division works closely with the Financial Management Division, which develops financial plans, monitors TIRZ balances, and aids in reviewing reimbursement requests. They also work with the City Attorney's Office who aid in negotiating and drafting agreements with developers. Additionally, the Mid-Town TIRZ helps fund other economic development incentives under the Center City Housing Incentive Policy (CCHIP), which is managed by Center City Development & Operations (CCDO) and economic development incentives under Chapter 380, managed by the Economic Development Department (EDD).

As of January 2020, The Mid-Town TIRZ portfolio included 37 projects. These projects include housing development, office and commercial space, parks, and public improvements/infrastructure. Total funding from the TIRZ is $117.4 million.

Audit Scope and Methodology

The audit scope included all projects within the Mid-Town TIRZ since inception.

To gain an understanding of the area under audit we interviewed department personnel, conducted reviews of relevant documentation, and developed process flows, and TIRZ financial data.

Testing criteria included Texas Tax Code Chapter 311, Mid-Town TIRZ Project and Finance plans, CCHIP program manual, & TIF policies and procedures.

For testing, we verified projects were appropriately approved including receipt of support documents. Additionally, we reviewed Contract Progress Payment Requests (CPPR's) for both TIF Division projects and CCHIP tax reimbursements separately. Further, we reviewed documentation to confirm an appropriate compliance program had been established. We reviewed the finance plan to verify it was accurate and supported. We verified reporting to the State Comptroller was accurate and timely. Finally, we verified communication was adequate and fee collection was accurate.

We determined that the following internal control components were significant to the audit objective. Significant internal control components and principles include the following:

Component	Principle
Control Environment	Board of Directors demonstrates independence from management and exercises oversight
Control Activities	The organization selects and develops control activities that contribute to the mitigation of risks
	The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.
Information & Communication	The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.
	The organization internally communicates information necessary to support the functioning of internal control.
	The organization communicates with external parties regarding matters affecting the functioning of internal control.

We relied on computer-processed data in SAP to review and confirm actual payments and fee collection. Our reliance was based on performing direct tests on the data rather than evaluating the system's general and application controls. We do not believe that the absence of testing general and application controls had an effect on the results of our audit.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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.

Audit Results and Recommendations

A. Administrative Processes

A.1 NHSD & Mid-Town TIRZ Finance Plan

NHSD has adequate administrative processes in place. NHSD is required to report the status of the Mid-Town TIRZ to the Texas State Comptroller on an annual basis. We tested fiscal years 2018 and 2019 and confirmed that the data provided was accurate and timely.

In addition, NHSD is adequately collecting fees due to the City of San Antonio for administration of the Mid-Town TIRZ. Staff have accurately collected approximately $838,000 in fees since 2009.

Finally, the Mid-Town TIRZ finance plan is accurate and up-to-date. All projects are appropriately included in the finance plan. In addition, amounts associated with each project are accurate and supported. Further, actual payments to developers match SAP and the tax increment is accurate and matches SAP.

A.2 Center City Development Office (CCDO)

The Mid-Town TIRZ Board of Directors approved participation in the Center City Housing Incentive Program (CCHIP). CCHIP provides incentives to housing projects, including affordable housing, within targeted growth areas. The Mid-Town TIRZ provides funding of CCHIP incentives, primarily tax reimbursements, within the zone.

CCDO's administrative management of CCHIP projects that are receiving funding via the Mid-Town TIRZ is adequate. We tested 5 projects between FY2017 – December 31, 2019 and determined appropriate approvals were obtained, support documents were received, and the developer is only receiving funding from the Mid-Town TIRZ via a single program.

In addition, we found controls over tax reimbursements were adequate. We tested a sample of 20 tax reimbursements for 10 projects. We found the reimbursements contained required support documents, no duplicate payments existed, and accurate payments were posted in SAP.

Finally, we determined that compliance over CCHIP programs was sufficient. All projects had a contract administration plan, quarterly progress reports were obtained, and supporting documents were received per the contract.

Recommendations

None.

B. Project Approvals

NHSD is not executing their established approval process. Of the 11 projects we reviewed, 3 projects did not obtain all required support documents including project pro formas and financial statements.

Per NHSD's TIRZ funding application process, a series of support documents are required to be submitted with the developer's application to include detailed sources and uses, financial statements, project pro formas, project summary, site plans, and other relevant documentation.

NHSD has not consistently enforced the submission of support documents from developers. The status of projects at the time of application submission varies widely from developer to developer, which affects whether or not they submit some support documents.

However, without required support documentation, COSA staff and the Mid-Town Board of Directors cannot make fully informed decisions about the appropriate funding levels for projects. Given the level of funding for some projects, obtaining complete information is necessary to reduce the risk of overfunding projects.

Recommendation

The Director of NHSD should ensure developers submit and staff receive all required support documentation prior to reviewing applications and document any exceptions.

C. Contract Progress Payment Requests (CPPR)

C.1 Inefficient CPPR Approval Process

The CPPR approval process is inefficient. For the 21 CPPRs we reviewed, it took an average of 120 days, or approximately 4 months, from the time of submission to payment to developer.

A CPPR is routed for review and approval up to 16 times, with at least 10 different signatures. Some CPPRs require approval by the Mid-Town Board of Directors prior to payment, which increases processing time.

Per the 2008 TIF Guidelines, the City reviews all requests for tax increment funds, including reimbursement invoices, for compliance with provisions of the Project

Plan, Financing Plan, Development Agreement, and Interlocal Agreement(s) and presents such requests for payment to the TIRZ boards for approval prior to making distributions. All disbursements must be approved by the Mid-Town TIRZ Board of Directors via ordinance.

An inefficient review and approval process increases CPPR processing times, which increases the risk of controls not working as intended. As such, 25% of the CPPRs we reviewed were missing at least one signature, but were still approved.

C.2 Agreement Effective Date

The effective date of agreements should be refined. Upon review, we found 3 invoices that were paid for work that occurred after City Council approval, but before the final signature on the agreement and 1 invoice that was paid for work that occurred prior to City Council approval, totaling $38,615.

The final step in a project being added to the TIRZ is approval by City Council. Per the developer's agreements, the contracts become effective on the date of the last signature on the agreement. However, some agreements have several months between City Council approval and the final signature on the agreement. Further, per the 2008 TIF guidelines, costs incurred prior to the date of execution of a development agreement are not eligible for reimbursement.

Without a clear effective date, NHSD increases the risk of reimbursing non-reimbursable costs. In addition, contractors could perform work that becomes ineligible for reimbursement for administrative reasons, interfering with the goals of the City of San Antonio, the Mid-Town TIRZ, and the developer.

Recommendation

The Director of NHSD should:

C.1 Review and streamline the CPPR approval process including how responsibilities in the review process can be consolidated to improve processing time. The NHSD Director could consider a tiered approach to approval based upon a desired threshold.

Understanding that a change in the disbursement process would require an ordinance change, consider approaches to streamline the board approval process for CPPRs which could aid in decreasing processing times.

C.2 Work with the City Attorney's Office to clarify the effective date of future agreements.

D. Monitoring Process

Compliance monitoring is not adequate for Mid-Town TIRZ projects. Contract administration plans had not been developed for the 4 projects we reviewed. Three projects within the Mid-Town TIRZ have not begun construction yet, which would trigger additional monitoring. Of the projects that have begun construction, the TIF Division have performed no or limited monitoring for insurance, progress reports, and prevailing wage requirements. In addition, while site visits have occurred, they have been infrequent.

Per each agreement, developers must maintain various compliance elements including adequate insurance, pay and performance bonds, and quarterly progress reports during construction.

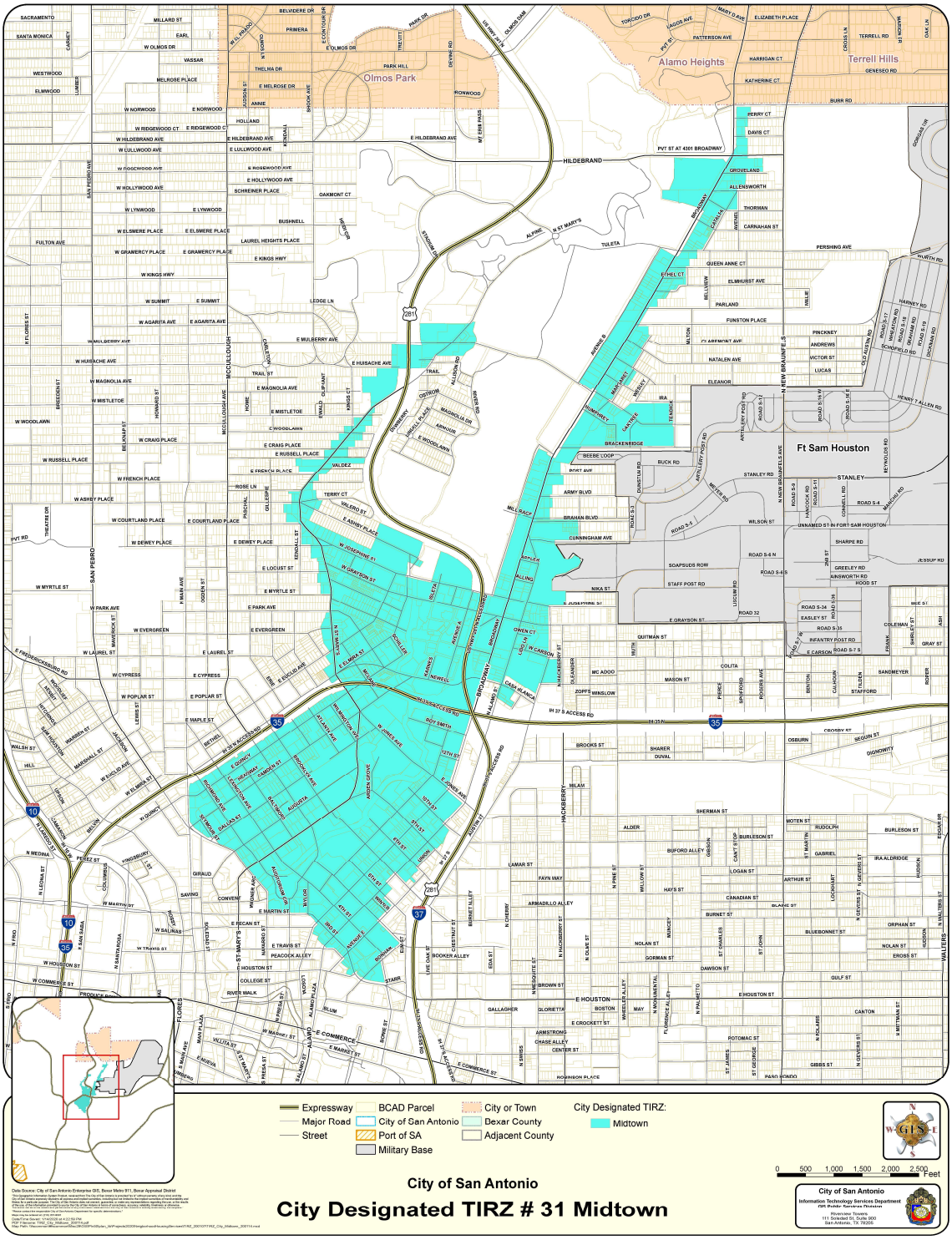
NHSD has not established a compliance monitoring program. Without adequate compliance monitoring, COSA is at risk of financial loss or not achieving project goals.

Recommendation

The Director of NHSD should establish a compliance monitoring program for TIRZ Projects. In addition, NHSD should evaluate allocation of resources to effectively develop a program and monitor compliance for TIRZ projects.

Appendix A – Supplemental Information

Figure 1 – Map of City-Designated TIRZ # 31



Appendix B – Staff Acknowledgement

Baltazar Vargas, CIA, CFE, Audit Manager
Nastasha Leach, CIA, CGAP, Auditor in Charge
Hedei Newcomb, CFE, Auditor

Appendix C – Management Response

CITY OF SAN ANTONIO

SAN ANTONIO TEXAS 78283-3966

July 31, 2020

Kevin W. Barthold, CPA, CIA, CISA
City Auditor
San Antonio, Texas

RE: Management's Corrective Action Plan for audit of NHSD Mid-Town TIRZ

Neighborhood & Housing Services has reviewed the audit report and has developed the Corrective Action Plans below corresponding to report recommendations.

Recommendation					
#	Description	Audit Report Page	Accept, Decline	Responsible Person's Name/Title	Completion Date
1	**Project Approvals** Ensure developers submit and staff receive all required support documentation prior to reviewing applications and document any exceptions.	5	Accept	Edgar Olivas TIF – Economic Development Manager	July 1, 2020
	Action plan: The TIF Division established a Steering Committee that is comprised of City Attorney's Office staff, Finance Management Division staff, and TIF staff to review all submitted TIF Funding Applications. The Steering Committee reviews all applications to ensure supporting documents are included.				
2	**Contract Progress Payment Request (CPPR)** • Review and streamline the CPPR approval process including how responsibilities can be consolidated to improve processing time • Work with the City Attorney's Office to clarify the effective date of future agreements	5	Accept	Edgar Olivas TIF – Economic Development Manager	December 31, 2020

Recommendation					
#	Description	Audit Report Page	Accept, Decline	Responsible Person's Name/Title	Completion Date
	Action plan: A process flowchart has been created to help determine where improvements can be made. The TIF Division will meet and discuss with City Attorney's Office and Finance Management Division the process flowchart so that a more efficient process can be established. The TIF Division is working with the City Attorney's Office to clarify effective dates of agreements.				
2	**Compliance Monitoring** Establish a compliance monitoring program for TIRZ projects. In addition, NHSD should evaluate allocation of resources to effectively develop a program and monitor compliance for TIRZ projects.	6	Accept	Edgar Olivas TIF – Economic Development Manager	December 31, 2020
	Action plan: Cap Administration Plans have been developed for all Midtown TIRZ projects. A creation of a database is being considered, which will help in running monthly reports for compliance deliverables.				

We are committed to addressing the recommendations in the audit report and the plan of actions presented above.

Sincerely,

R Soto

8-7-20

Verónica R. Soto, FAICP
Director
Neighborhood & Housing Services

Date

8/7/2020

Lori Houston
Assistant City Manager
City Manager's Office

Date