CITY OF PHILADELPHIA PENNSYLVANIA

OFFICE OF THE CONTROLLER

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COMMERCE DEPARTMENT

Review of the
Cultural and Commercial Corridors Program

October 2012

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November 13, 2012

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Pursuant to Section 6-400(d) of the Home Rule Charter, the City Controller's Office conducted a review of the Commerce Department's Cultural and Commercial Corridors Program to determine whether the Commerce Department had designed and placed into operation procedures that ensured adequate oversight of program spending, including effective use of the bond proceeds. A synopsis of the results of our work, which was performed in accordance with *Government Auditing Standards*, is provided in the executive summary to the report. The conditions noted in this report occurred under the administration of the previous Commerce Director when most of the Cultural and Commercial Bonds proceeds were committed to funding various projects under the Program.

We discussed our findings and recommendations with your staff at an exit conference and included your written response to our comments as part of the report. We believe that our recommendations, if implemented by management, will improve the efficiency and effectiveness of programs administered by the Commerce Department. Our recommendations have been numbered to facilitate tracking and follow-up in subsequent years.

We would like to express our thanks to you and your staff for the courtesy and cooperation displayed during the conduct of our work.

Very truly yours,

ALAN BUTKOVITZ
City Controller

cc: Honorable Michael Nutter, Mayor
Honorable Darrell L. Clarke, President
and Honorable Members of City Council
Members of the Mayor's Cabinet

Commerce Department
Review of the
Cultural and Commercial Corridors Program

Executive Summary

Why The Controller's Office Conducted The Examination

Pursuant to Section 6-400 (d) of the Philadelphia Home Rule Charter, the City Controller's Office conducted a review of the Commerce Department's Cultural and Commercial Corridors Program funded by $135.5 million of revenue bonds issued by the Philadelphia Authority for Industrial Development in December 2006. The objectives of our review were to determine whether the city's Commerce Department had designed and placed into operation procedures that ensured adequate oversight of program spending, including effective use of the bond proceeds.

What The Controller's Office Found

The Commerce Department did not provide adequate oversight of the Cultural and Commercial Corridors Program. We found that program goals and objectives were not defined, and measurable criteria were not established. The lack of defined goals and objectives and performance measures prohibited the Commerce Department from evaluating the outcome of specific projects and the program as a whole.

We also observed that grant agreements with award recipients did not contain requirements that would properly safeguard public funds. Organizations that received grants to distribute to other agencies (i.e., to administer sub-grants), were not required to publicly announce award opportunities. Grant agreements with other award recipients did not require documenting the use of a competitive bidding process.

Additionally, Commerce did not maintain adequate records documenting its monitoring of the projects. There were no records of any site visits made by Commerce personnel. Our review of project payments also indicated that the Commerce Department did not always properly scrutinize the documentation supporting the expenditure of bond funds. At times, vendor invoices submitted for payment provided insufficient detail to determine whether the expenditure was appropriate for the project. Because of these shortcomings, it is questionable as to whether taxpayer funds were spent in the most economical and effective manner as possible.

What The Controller's Office Recommends

The Controller's Office has developed a number of recommendations to address these findings. Some of the more significant recommendations made to the Commerce Department include: (1) establish clear goals and objectives that are tied to quantifiable performance measures; (2) require publicly advertising grant opportunities; (3) require the use of city competitive bidding procedures before expending the funds – these requirements should be extended to recipients of public funds through their grant award agreements; (4) do not use the revolving loan pool funds for grant awards; (5) conduct and document site visits of award recipients; and (6) require adequate supporting documentation when reimbursing award recipient requests.

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BACKGROUND INFORMATION

Overview

The Cultural and Commercial Corridors Program was created to improve and enhance the city's cultural and commercial corridors for the benefit of city residents. To achieve this objective, the program provided capital funding (in the form of grants and / or loans) to targeted cultural and commercial organizations which met certain criteria broadly described in the authorizing ordinance.[1]

Philadelphia based non-profit organizations, whose mission substantially focused on the arts and cultural activities, and which met other eligibility criteria, applied for and received city funding for various capital and infrastructure projects. Funding priority was given to organizations located within the city's cultural corridors which included: the Avenue of the Arts, the Benjamin Franklin Parkway, the Centennial District, the Historical District, and El Centro de Oro.

Applications were reviewed and awards were made by panels consisting of representatives from various city departments including: City Council, the Office of the City Representative and the Director of Commerce, the Managing Director's Office, the Office of the Director of Finance and the Mayor's Office.

Funding was also provided to revitalize commercial corridors throughout the city under the ReStore Philadelphia Corridors Program. The intent of this program was to re-establish the historic roles of commercial corridors as central places to shop, to work and to meet neighbors. Commercial corridor enhancements included capital and streetscape improvements, property acquisition and demolition, redevelopment grants, business support and technology improvements, and loan guarantees.

Projects were selected using an inter-agency process which included the Mayor's Office, the Commerce Department, the City Planning Commission, the Managing Director's Office, the Office of Housing and City Council.

Program Funding

The majority of program funding, which Commerce Department officials asserted was committed under the previous administration, was provided by the proceeds of the Cultural and Commercial Corridors Program Revenue Bonds (the bonds) issued in December 2006. The Philadelphia Authority For Industrial Development (PAID) sold the bonds in an aggregate principal amount of $135,515,000. The bond issue, scheduled to be repaid over twenty-five years, was comprised of PAID Series 2006A and 2006B, which were issued in the amount of $126,150,000 and $9,365,000, respectively, with the Series 2006A bonds being federally tax-exempt. Conversely, the Series 2006B bonds were deemed taxable. Interest rates on the Series 2006A bonds ranged from 4.00 to 5.00 percent, and from 4.89 to 5.17 percent on the Series 2006B bonds.

[1] Bill No. 060692, signed November 6, 2006.

The bonds were authorized by an ordinance[2] which also authorized a Service Agreement between PAID and the city requiring the city to pay the debt service on the bonds. PAID received an initial administrative fee of $150,000, and an annual administrative fee of $225,000 from April 1, 2007 through January 1, 2010 per the terms of the agreement. In addition to the bond proceeds, financial support for the program was also provided by the federal Community Development Block Grant, state funds and the city's General Fund.

The Philadelphia Industrial Development Corporation (PIDC) manages the daily affairs of PAID under the direction and governance of the five member PAID Board appointed by the mayor. Commerce and PIDC were primarily responsible for the oversight of the bond funds. The Pennsylvania Department of Transportation (PennDOT) and the Streets Department provided oversight for certain streetscape projects receiving funding from the bonds.

[2] Ibid.

COMMERCE'S OVERSIGHT OF CORRIDOR PROGRAMS WAS INADEQUATE

The Commerce Department (Commerce) did not provide adequate oversight of the Cultural and Commercial Corridors Program. Program goals and objectives were not clearly defined, and measurable criteria were not established to allow the Commerce Department to evaluate each project's outcome. We observed that grant agreements with award recipients did not contain requirements to properly safeguard public funds. Moreover, Commerce did not maintain adequate records documenting its monitoring of the projects. There were no records of any site visits or project inspections made by Commerce personnel. Finally, our review of project payments revealed that the Commerce Department did not always properly scrutinize the documentation supporting the expenditure of bond funds. We observed vendor invoices submitted for payment by the Commerce Department which provided insufficient detail to assess whether the expenditure was appropriate for the awarded project. Because of the above shortcomings in the corridor bonds program, one could question whether taxpayer funds were spent in the most economical and effective manner possible.

Program Goals And Objectives Were Not Clearly Defined and Measured

The ordinance that authorized the Cultural and Commercial Corridors Program stated that the purpose of the bonds was to finance the costs of:

> "improving and enhancing (a) the City's cultural corridors by providing funding to cultural institutions for capital improvements and other activities to improve the cultural corridors for the benefit of the residents of the City; and (b) the City's commercial corridors by providing funding for streetscapes; redevelopment projects; renovations; property acquisitions for redevelopment; technology equipment and upgrades; loan guarantees; demolition of blighted properties; and other activities to improve the commercial corridors for the benefit of residents of the City." [3]

Commerce Department officials asserted that certain program goals were accomplished, such as achieving a high level of minority business participation and providing the necessary financing for projects that may not otherwise attract funding from donors. However, our review of the program revealed the stated intent of improving and enhancing the corridors was described only in broad terms, and lacked specific program goals and objectives, making it difficult to validate management's statement. Furthermore, the absence of clear and measurable goals and objectives prohibited Commerce from measuring the outcome of specific projects, and ultimately the success or failure of the overall program.

For example, eighteen projects, including renovations to coffee shops, restaurants and retail stores along the city's commercial corridors, received awards averaging $42,000 each.[4] The Commerce Department, however, did not develop specific, measurable criteria that would allow it to evaluate the effectiveness of each project's outcome. In at least one instance, we determined that the grant awardee was no longer in business.

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[3] Ibid.
[4] See Appendix III for a listing of these projects and award amounts.

We also reviewed a $3 million award made to New Freedom Theatre (NFT). The theater ultimately received $2.2 million which was used to pay a portion of the theater's outstanding debts: $1.5 million to PNC Bank,[5] $307,000 to the Internal Revenue Service, $65,000 to PECO Energy, $40,000 to the Philadelphia Gas Works, $16,000 to the city's Water Revenue Bureau, and $280,000 to the NonProfits Assistance Fund. Even though this project represented a much larger investment of taxpayer funds, the Commerce Department again did not establish the criteria necessary to gauge its effectiveness.

Funding for the NFT award came from the taxable portion of the bond issue, which had few restrictions on its use. The $2.2 million award appeared to enable the theater to remain in operation. The theater undoubtedly improved its financial position by receiving the grant.

Our review indicated that there were no plans, agreements, or other evidence indicating how the theater intended to avoid future financial difficulties, or, for that matter, how the Commerce Department was going to measure the ongoing viability of the theater. Additionally, Commerce did not design indicators that would show whether the theater project was actually improving and enhancing this particular corridor for the benefit of city residents as intended by the program.

We noted the only requirement placed on NFT was to substantiate that the funding provided was used to pay these debts. Our review of documentation showed that subsequent to the $2.2 million award, the city's Commerce Department wrote to the NFT indicating that the theater had not substantiated its use of the funding in a timely manner. As a result, a second phase of the grant totaling approximately $800,000, was not awarded to the theater, and the funding was redirected to other projects.[6]

Recommendation:

We recommend that for future programs, the Commerce Department develop specific and measurable goals and objectives to monitor and evaluate program effectiveness. The measures developed should be quantifiable and tie back to the intent of the program. Funding should be directed only to projects which can reasonably be expected to achieve successful outcomes [204211.01].

Proper Safeguards Against Misuse of Funds Were Not Established

Because the Commerce Department did not establish proper safeguards over the use of the corridor bond funds, it placed these funds at risk for the occurrence of fraud, waste, or abuse. Furthermore, documentation we observed raised concerns about the fairness, openness, and competitiveness of the awards and bidding processes. The results of our work revealed the following conditions giving rise to our concerns.

[5] Documentation we reviewed indicated the NFT had incurred this debt for various capital improvements.
[6] Subsequent to our fieldwork, we observed correspondence that in 2010 NFT received an additional award of $250,000 for capital improvements.

ReStore Retail Incentive Grant Program

The Merchants Fund (TMF), a non-profit organization, received a grant from the ReStore Philadelphia Corridors Fund to create and administer the ReStore Retail Incentive Grant Program. This program provided funding to businesses for capital costs that "fitted out" and equipped interior spaces for new retail uses, and TMF received two grants of $500,000 to administer.[7]

Although entrusted to administer $1 million of city grant funds, TMF's director was the organization's only employee.[8] She was solely responsible for maintaining the checkbook, bank accounts and accounting records, signing and authorizing checks, and reconciling the accounts. She informed us that no countersignatures were required on the checks.

Adequate segregation of duties is a hallmark of good procedures to safeguard against misuse of funds. The tasks of handling an asset, recording it in the books, and performing other accounting functions should not be completed by the same individual because it increases the risk of errors occurring and going unnoticed and uncorrected. Furthermore, inadequate segregation of duties could allow an employee to commit and conceal a theft or fraud. Although our review found no errors or improprieties, we question the soundness of Commerce's decision to use a small organization having only one employee to administer $1 million in grant funds.

Our examination also revealed that city corridor bond funds were commingled with other funds administered by TMF. This practice could compromise the integrity of city funds in the absence of an adequate audit trail. Although maintaining funds in segregated bank accounts would strengthen controls over these funds, there was no requirement in the contract with TMF to keep the funds segregated. We did observe, however, that the director eventually opened money market accounts and transferred the unspent corridor bond grant funds to those accounts.

TMF's administration of the ReStore Retail Incentive Grant Program included disseminating information about the program to businesses, which had an interest in applying for these grant funds. Rather than publicly advertising the Retail Incentive Grant Program opportunities in print or radio ads, TMF used a private e-mail list. We observed documentation indicating that TMF sent approximately 170 e-mail notifications to members of community development corporations, small business development centers, and other agencies. When we asked TMF for the list of e-mail recipients, we were told the list was "dynamic" and could not be reproduced. In justifying its use of a closed e-mail list to notify businesses of this program, TMF asserted that based on past experience, the notification would likely be passed along to many other interested parties by the initial e-mail recipients. Inspection of the sign-in-sheets indicated 119 individuals attended the public meeting for the first round of grant awards, and 104 individuals attended the second round.

We question the transparency and competitiveness of announcing the ReStore Retail Incentive Grant Program by using a closed listing, rather than a method more open to the public, such as newspaper or radio advertisements. By potentially limiting the grant funding to a select group of

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[7] See Appendix II for the eligibility requirements established by the city for TMF's use when making subgrants.
[8] However, she is only one of the members of the program committee that evaluates the projects requesting grants.

people, the risk of fraud, waste, or abuse occurring was increased. We believe the requirements for public notification should have been established in the award agreement with TMF. We also noted that, following two rounds of awards, approximately $190,000 in grant funds were still being held by TMF to be awarded in the future.[9]

The last observation we made in our review of TMF related to the director's notes summarizing the program committee's evaluation of the businesses that requested funding. We were troubled by a notation in the description of the Bloo Leaf Café proposal stating "[the project was] earmarked to fulfill a political obligation for the Commerce Department. The company plan is so weak so we will probably have to bundle consulting with it to protect the investment." We inquired about the meaning of that statement, and TMF's director informed us that "geography was a consideration" in making the awards, and that no grants had been awarded in the councilmanic district where the Bloo Leaf Café was to be located. She also noted that since this project was not completed, the grant was never provided.

<u>Recommendations</u>:

To establish safeguards against the misuse of taxpayer funds, we recommend that, in the future, the Commerce Department take the following actions for similar programs:

- Consider screening organizations which administer taxpayer funds to determine whether they have sufficient staff size to mitigate the possibility of needlessly exposing the funds to loss through theft or defalcation [204211.02].

- Include a requirement in all future contracts that organizations administering taxpayer funds maintain those funds in separate bank accounts to preclude commingling them with other assets under their control [204211.03].

- Require that information pertaining to available grant program funding be disseminated to interested parties in an open, transparent, and competitive manner. Examples include the use of public media such as newspaper or radio advertisements and the internet [204211.04].

- Refrain from considering or earmarking grant awards in order to fulfill political obligations [204211.05].

Gap Financing Loan Pool

Corridor bond funds were also used to establish the Gap Financing Loan Pool, a program to provide sub-grants and low interest loans to assist in acquisition and development activities along the city's commercial corridors. The Reinvestment Fund (TRF), a non-profit organization, was selected to administer an $8.5 million award. As the loans were repaid, TRF was to use the proceeds and interest to create an on-going resource to finance future development projects in neighborhood commercial corridors.

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[9] See Appendix III for a listing of ReStore Retail Incentive Grant Program awards made by TMF.

Thirteen projects received loans ranging from $100,000 to $1,000,000 for renovations or new construction of properties along the commercial corridors.[10] TRF indicated that the primary method used to inform the development community about the loan program was a Gap Financing Program "request for proposal" posted on the city's website. We were also informed that TRF reached out to active and potential borrowers by word of mouth. Documentation provided by TRF indicated they reviewed 75 applications for requests totaling over $60 million.

Our review of projects that received funding from the Gap Financing Loan Pool indicated that two sub-grantees received especially favorable terms. TRF entered into contracts with Progress Trust, a developer, and Broadnu Enterprises, parent company of an existing supermarket, to complete construction of a new supermarket, parking deck, and other site improvements at North Broad and Oxford Streets. The terms of these two agreements essentially provided for forgiveness of both a $500,000 loan to Progress Trust, and a $1 million loan to Broadnu Enterprises, if the supermarket was completed by June 30, 2010. On that date, both loans were forgiven by TRF.

We observed that eleven other project agreements we reviewed provided funding through low interest loans, prompting us to ask TRF management why Progress Trust and Broadnu Enterprises received grants. We were referred to an analysis prepared by TRF that indicated Progress Trust would not have been able to meet the debt service requirements during the startup and construction phase of the project. The analysis also recommended a grant to Broadnu Enterprises, because the supermarket had to service a higher debt load than similar stores.

We did not consider the stated justification for forgiveness to be well-founded. Both Progress Trust and Broadnu Enterprises had arranged for other significant grants and low interest loans as an incentive to undertake the project, yet TRF made the evaluation that this for-profit business would be burdened by too much debt, and therefore, additional taxpayer funds should be gifted (granted) to make the project financially viable. Based on our review of the analysis provided by TRF, there was no investment of equity by Progress Trust, and Broadnu's investment of equity was slightly less than four percent of the project's cost. With such a small investment by the owners, it is obvious that any such project would carry a high debt burden.

Finally, we were informed that TRF accepted the proposals because the community needed both a supermarket and the jobs it would create. However, the condition for debt forgiveness established by TRF simply required that the supermarket be developed and opened by the stated date. We believe that any debt forgiveness should have been contingent upon the supermarket and related jobs being maintained over a stated period of time. Such a condition would not have been unreasonable for a project funded primarily by taxpayers, especially in light of the fact that the bond issue will not be repaid until December 2031.

We do not believe this award resulted in the most efficient use of taxpayer funds because TRF's decision to forgive this debt ensured that $1.5 million, or 18% of the amount entrusted to TRF, would not be recouped by the Gap Financing Loan Pool to be used for future community development projects. By contrast, a $1 million loan to Philabundance reportedly allowed the organization to triple its storage capacity for refrigerated food that will be distributed to the

[10] See Appendix IV for a list of Gap Financing Loans and recipients.

needy, and will further serve to benefit the community as the loan is repaid and the funds are directed to other projects.[11]

Recommendation:

To maximize the benefit of revolving loan pool funds as an on-going financial resource for development within the commercial corridors, we recommend that, in the future, funds be awarded as loans and redistributed to other qualified projects as they are repaid, rather than being forgiven [204211.06].

Streetscape Projects and Cultural Award Fund

The planned revitalization of commercial corridors included streetscape enhancements and capital improvements funded by corridor bond proceeds. These funds were used for a broad range of improvements on or around city streets, including street lighting, street and sidewalk paving, crosswalks, public signage, greening and trees, and utility placement, as well as planning, design, architecture, and engineering studies. Thirty streetscape projects were planned, each needing an architectural firm for design work.

After observing that all thirty projects were divided among only three architectural firms, we questioned the Commerce Department regarding its process for bidding and selecting the firms that performed the work. We were informed that the Commerce Department and PIDC requested architectural firms to provide resumes illustrating their previous work. The Commerce Department and PIDC selected three firms based on the resumes submitted, and divided the projects among the firms based on what was believed to be the best match of skills

Because the corridor bonds were issued by PAID, the Commerce Department was not required to follow city bidding procedures in selecting the architectural firms. Nevertheless, we inquired why the Commerce Department did not solicit bids as doing so would aid in safeguarding public funds and increase the probability of a fair and competitive award process. The Commerce Department asserted that bids were not solicited because of the time constraint of spending the funds within three years, and the priority placed on completing the projects.[12] The Commerce Department also mentioned that the Streets Department retained an outside firm to review the quality of work and the cost of the projects.

We question the Commerce Department's position that city bidding processes could not be followed. In prioritizing these projects, consideration should have been given to ensuring that the taxpayers' interests were served by obtaining the necessary services at competitive prices. The award process used for the design of the streetscape enhancements, however, resulted in a limited number of participants receiving bond funding. Although an outside project management firm was used to control costs, requiring a formal bid for each project, in our opinion, would have helped ensure the most economical costs to the taxpayers.

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[11] "Philabundance Hunger Relief Center," PhilabundanceNews, Winter 2010.

[12] However, at the exit conference, Commerce Department officials informed us that the architectural firms were also screened through a selection process which required the firms to respond to a formal Request for Qualifications.

In a related matter, the Commerce Department did not always require recipients of corridor bond funds to competitively bid projects. For example, we noted that requirements were not placed on the recipients of the smaller, cultural fund awards to document that a competitive bidding process was used when contracting work to complete their funded projects.

Although most recipients we interviewed claimed they obtained quotes for the work, only a few actually maintained records of the quotes they obtained. The Commerce Department did not require that a formal, bidding process be documented and retained. As a result, little assurance was provided that the public funds achieved the maximum impact for the least cost.

Recommendations:

We recommend the Commerce Department follow city procurement policies, including bidding requirements, regardless of the funding source, time constraints or priorities associated with similar future projects [204211.07]. We also recommend the Commerce Department require all sub-recipient organizations receiving public funds to follow the same city procurement policies, including those related to the solicitation of bids and the retention of documentation [204211.08].

Records Documenting Monitoring Of Project Expenditures Not Maintained

During the audit, we asked to observe any records, logs, or other supporting evidence which documented site visits by Commerce Department employees to monitor the renovations and improvements that were made. The Commerce Department informed us that no records were maintained indicating the dates, purpose, or reasons for site visits. The representative in charge of the cultural corridor improvements noted that site visits only occurred if a particular project was experiencing difficulties. During our discussions with the director of TMF, we were told that she never saw a representative from the Commerce Department after the award process was completed.

In our opinion, the Commerce Department’s failure to maintain records of its site visits is a significant control weakness. Project monitoring is an important safeguard to ensure that all contractually agreed-upon work was performed in a timely manner and in accordance with the applicable standards. Without physically observing on-going projects on a regular basis, the Commerce Department denied itself the opportunity to determine whether any instances of misuse, waste, or fraud involving the bond funds occurred.

Recommendation:

Good oversight procedures and basic project management require that site visits be made to monitor compliance with contract terms. We therefore recommend that the Commerce Department periodically conduct and document the results of site visits. More costly and higher risk projects should receive a more detailed review, and an assessment regarding the reasonableness of the project’s cost should be made for each project [204211.09].

Support for Bond Expenditures Not Always Properly Scrutinized

Our review of project invoices indicated the Commerce Department approved some payments without adequate supporting documentation or scrutiny. Some requests for reimbursement lacked documentation, such as a packing slip, that would clarify the nature of the expense. We also observed invoices that were paid even though adequate detail was not provided to determine the goods or services that were received.

For example, as part of a $30 million project of the cultural corridors program, an architect was engaged by the Philadelphia Museum of Art to design a new loading dock and art handling area. This project reportedly allowed the old loading zone to be reopened and restored to its original purpose as a street-level visitor entrance.[13] In reviewing expenditures for this project, however, we observed redacted invoices submitted by the Art Museum that concealed the billing details – the hours worked and the rates charged – for work performed by the architectural staff contracted for a project.[14]

In response to our inquiries, we were told by the Art Museum director that the architecture firm's contract had a confidentiality agreement prohibiting the release of the hourly rates of its staff, and the original invoices were maintained at the Art Museum for review. We obtained and reviewed the original invoices, and noted no discrepancies between the totals billed and the supporting detail that was hidden.

However, by approving the above reimbursements with inadequate support, the Commerce Department did not ensure the payments were appropriate. Best practices dictate that expenditures being processed for reimbursement be properly substantiated. When invoices and other submitted documentation do not contain sufficient detail to indicate the payment is proper, the request should be rejected until adequate documentation is received.

Recommendation:

The Commerce Department should require that all future invoices and related supporting documentation adequately substantiate the expenditures related to the reimbursement request [204211.09]. We also recommend that confidentiality agreements not be placed in future contracts funded by city dollars, as these transactions must be available for public review [204211.10].

Conclusion

A lack of Commerce Department oversight and monitoring, coupled with the absence of clear program goals and measures created opportunities for questionable spending, possible misuse of funds, and the inability to measure the success or failure of the city's $135.5 million Cultural and Commercial Corridors Program. In our opinion, the inadequacies we identified may have precluded the Commerce Department from fully achieving the program objectives, which were

[13] John Steele, "Art Museum's underground expansion gets underway," flying kite, December 14, 2010, <http://www.flyingkitemedia.com/devnews/artmuseumexpansion1214.aspx>.
[14] See Appendix V for an example of a redacted invoice.

to improve and enhance the city's cultural and commercial corridors for the benefit of city residents.

Decisions were made to forgive loans, which were meant to be paid back and re-used to provide other organizations with cultural and commercial development opportunities. We also observed weaknesses in procedures to identify potential candidates eligible for grant awards and in the process for awarding streetscape enhancement projects. These weaknesses may have thwarted the ability of the Commerce Department to attract better projects and achieve the most economical costs of the enhancements.

If the remaining unspent funds of the Cultural and Commercial Corridors Program are to be spent wisely, Commerce Department management must begin providing more proactive program oversight and monitoring. It must also establish quantifiable goals and objectives to gauge the success or failure of the program.

APPENDIX I: OBJECTIVES, SCOPE, AND METHODOLOGY

The Controller's Office conducted a review of the Cultural and Commercial Corridors Program. The program, which was funded in part by taxable and tax-exempt bonds, was created to improve and enhance the city's cultural and commercial corridors. The objectives of our review were to determine whether the city's Commerce Department had designed and placed into operation procedures that ensured adequate oversight of program spending, including effective use of the bond proceeds.

To gain an understanding of the procedures that the city's Commerce Department had designed and placed into operation over the Cultural and Commercial Corridors Program, we:

- Interviewed management of the Commerce Department and PAID regarding the processes in place for awarding, and monitoring the expenditures of bond funds.

- Made inquiries of grant recipients concerning the processes for making sub-grant awards, and the bidding processes used for work paid with bond funds.

- Reviewed the authorizing ordinance, the official statement, and closing documents for the Cultural and Commercial Corridor Bonds.

- Obtained and reviewed the contract agreements for selected grant recipients.

- Obtained and reviewed invoices and other supporting documentation for selected expenditures.

We performed our work from July 2011 through May 2012 in accordance with *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.

APPENDIX A

PROJECT ACTIVITIES AND SPECIAL CONDITIONS

A. **Project Activities:** The GRANTEE will use Program funding to undertake a project consisting of the establishment and administration of the Retail Incentive Grant program ("RIG") to fund a portion of the costs of fitting out and equipping interior space for new and upgraded retail uses consistent with the strategy of the neighborhood commercial corridors and located on properties on or within one block of a commercial corridor in the City of Philadelphia. RIG will support corridor managers in attracting desired retailers or executing major upgrades to their corridors by assisting in cases where the fit out expenses of the appropriate space are beyond what can be reasonably covered by landlord or tenant.

The project to be supported with Program funding shall be limited to the following activities:

1. GRANTEE will provide sub-grants, in accordance with TMF standards, to eligible businesses and property owners entities to assist with capital costs of fitting out and equipping interior spaces for new retail uses consistent with strategy of the neighborhood commercial corridors;
2. GRANTEE will issue sub-grant applications; review responses; and select recipients adhering to the following Applicant and Project Eligibility Criteria:
    a. Eligible applicants include businesses located on neighborhood commercial corridors and owners of commercial and mixed use properties located on neighborhood commercial corridors. Site control is required.
    b. Sites must be located on or within one block of a neighborhood commercial corridor where a corridor revitalization strategy or a community plan is in place or under development by a corridor management organization (CDC, business improvement district, Main Street manager, or other). Applications must demonstrate that proposed business and fit-out project are consistent with that strategy.
    c. The anticipated sub-grant range is up to $50,000 and no more than 50% of a project
    d. Applicants must demonstrate that proposed fit-out projects are feasible.
    e. Funds must be used for capital costs of fitting out interior spaces. Examples of eligible costs are: electrical, HVAC, carpentry, plumbing, flooring, windows/doors, lighting, and permanent fixtures.
    f. Architectural plans must be in accordance with the appropriate standards for permitting and be approved by the City.
3. GRANTEE will develop and utilize a method of selecting sub-grant applications for

projects that meet the following criteria:

a. Desirability of type of business, as indicated by corridor strategy or community plan;

b. Demonstrated financial need;

c. Substantial job creation or maintenance notably for ex-offenders, welfare-to-work clients, new college graduates looking to settle in Philadelphia;

d. Supporting start-up or expansion of disadvantaged businesses;

e. Blight elimination;

f. Pedestrian-oriented design which conforms to existing CDC design criteria including respect for historic building attributes;

g. Demonstrable involvement of minority, women and disabled business owners, suppliers and/or contractors (MWDBE);

h. The potential for the business to succeed as demonstrated by past performance (existing business) or the business plan (new business);

i. The potential to enhance foot traffic and commerce for co-located businesses on the corridor—a keystone business;

j. Enhancement of a heritage business— a family-owned and operated company which is committed to the next generation and a renewed business paradigm for the 21st Century;

k. Demonstration of an e-commerce strategy where applicable;

l. Sustainable, green strategies, sensitivity and commitment: diminished waste or pollution, better use of energy, local sourcing, recycled products, recycled building products, etc;

m. Each business model will be tested for viability against appropriate industry standards.

4. GRANTEE will release sub-grant funds upon receipt of:

   a. Documentation that all non-City participation funds have been secured before sub-grant funds are dispersed

   b. Invoices, receipts, cancelled checks or other payment verification and color photographs of the completed work.

5. GRANTEE will monitor sub-grantees with regular visits and check-ins for 6 -12 months to assure that the business is stable after the construction project is completed. Scope includes, but is not limited to, routine review of finances, customer counts, merchandise review, marketing and advertising with an eye to course corrections and interventions as needed including referrals to appropriate consultants. Merchants will agree to this term in the sub-grant contract.

6. GRANTEE will provide requested reports to the City and PAID for record-keeping purposes only as the City and PAID will have no recourse with regard to this grant. GRANTEE will provide bi-annual reports to the City for five years from effective date

Project	Project Description	ReStore Grant Amount
D.P. Dough	Fit out space for calzone restaurant	$42,000
Gold Standard Café	Renovate space for comfort food restaurant	50,000
Lovers & Madmen Coffee Lounge	Café construction costs	24,110
Tiffin Pizza, Etc.	Expand pizza shop into adjacent space	40,000
The Trolley Car Café	Rehab public property for use as diner	50,000
Weaver’s Way Co-op	Renovate for food co-op use	50,000
The Wine Thief	Fit out space for restaurant/bar	46,000
Winnie’s Le Bus	Renovate established restaurant	12,000
Yards Brewing Company	Expansion of local brewery	30,000
The Village at 63rd Street	Renovate space for coffee shop	25,000
Eye Encounters	Expand eyewear business to new location	49,315
Guacamole MexGrill	Renovate space for Mexican restaurant	49,283
Manakeesh Café & Bakery	Rehab bank for Lebanese café and bakery	50,000
Mariposa Co-op	Relocate food co-op	50,000
Milkboy Coffee	Renovate for use as café	49,902
Mugshots Coffee House & Café	Expand coffee shop to new location	45,000
OPA Restaurant	Renovate Greek restaurant	50,000
Urban Jungle	Fit out irrigated greenery business	43,755
TMF Admin Fee		50,000
Total Expended ReStore Funds at 4/16/2012		806,365
Unspent Funds Held by TMF in money market accounts		193,635
		$1,000,000

SOURCE: Prepared by the Controller’s Office based on information provided by The Merchant’s Fund.

APPENDIX IV: LISTING OF GAP FINANCING LOANS AND RECIPIENTS

Project	Gap Financing Loan Amount ($)	Project Description	Recipient
Weaver’s Way	1,000,000	Convert Caruso’s Market building to food co-op	Glenn Bergman
Brinton House	113,496	Building renovation for coffee shop / café	Ken Weinstein
Progress Plaza Trust*	500,000	Renovation of retail shopping center	Wendell Whitlock
Fresh Grocer*	1,000,000	Construction of a full service supermarket	Pat Burns
Philabundance	1,000,000	Renovation of warehouse	Bill Clark
Schmidt’s Retail	1,000,000	Convert brewery to retail shopping space	Bart Blatstein
U3 Ventures	485,000	Tenant renovation for Milkboy coffee shop	Omar Blaik
Crane Old School	748,700	Old St. Michael’s School renovated to commercial space	David Gleeson
Grasso Holdings	1,000,000	Amalgamated Clothing Workers of America building converted to apartments / retail space.	David Grasso
Asian Arts	700,000	Property acquisition to develop multi-tenant arts facility.	Gayle Isa
Mariposa	475,000	Renovation of food co-op facilities.	Dan Ohlemiller
Mt. Airy USA	193,500	Convert blighted property to commercial space.	Jason Salus
Twelve 27, LLC	284,304	Renovation of blighted property to commercial space.	Andrew Alexander

*Loan Forgiven

SOURCE: Prepared by the Controller’s Office based on information provided by The Reinvestment Fund

Invoice

Gehry Partners, LLP
12541 Beatrice Street
Los Angeles, CA 90066

RECEIVED
JUN
By

May 31, 2007
Invoice No: 15261

COO
Philadelphia Museum of Art
Box 7646
Philadelphia, PA 19101-7646
United States

Project 2006005-000-GP200 Philadelphia Museum of Art - Gehry Partners (Time & Material)

Professional Services from May 1, 2007 to May 31, 2007

Phase 100 Concept Design

Professional Personnel *

	Hours	Rate	Amount	
Employee 1	[redacted]		24,200.00	
Employee 2			8,400.00	
Employee 3			8,400.00	
Employee 4			21,216.00	
Employee 5			8,713.25	
Employee 6			16,675.75	
Employee 7			20,496.00	
Employee 8			4,233.00	
Employee 9			16,971.50	
Totals			129,305.50	
Total Labor				129,305.50

Billing Limits	Current	Prior	To-Date
Total Billings	129,305.50	499,914.75	629,220.25
Limit			2,200,000.00
Remaining			1,570,779.75

Total this Phase $129,305.50

	Current	Prior	Total
Billings to Date	129,305.50	499,914.75	629,220.25

Total this Invoice $129,305.50

James Boyden 6/26/07 4100-MPF-6620

* **NOTE:** Employee names hidden by the Controller's Office.

CITY OF PHILADELPHIA

OFFICE OF THE DEPUTY MAYOR FOR ECONOMIC DEVELOPMENT
AND DIRECTOR OF COMMERCE
1515 Arch Street – 13th Floor
Philadelphia, PA 19102
(215) 683 - 4600
FAX (215) 683 - 4675

ALAN GREENBERGER
Deputy Mayor

November 9, 2012

Alan Butkovitz, City Controller
Office of the Controller
1230 Municipal Services Building
1401 John F. Kennedy Boulevard
Philadelphia, PA 19102-1679

RE: Review of the Cultural and Commercial Corridors Program dated September 12, 2012

The City of Philadelphia's Department of Commerce (Commerce), representing the many members of the Cultural and Commercial Corridors Bond Program Team, wishes to respond to the City of Philadelphia Office of the Controller audit titled "Review of the Cultural and Commercial Corridors Program." Although not stated in the title, it appears that the intent of the audit report was to review the operations procedures of the program only as they relate to the Department of Commerce, not the entire team including the Office of the Controller. As a result, the audit only addresses the negative findings of the Department of Commerce's program monitoring; it steers clear of any mention of our operating procedures. Therefore, I am happy to use this opportunity to provide a more comprehensive review of the program.

In this response, the Department of Commerce will 1) present a full picture of the program and its accomplishments to date; 2) respond to the findings, with a more complete description of the interagency operations procedures; and 3) raise concern with the procedures of the Office of the Controller with regard to the conduct of this audit.

1) The Cultural and Commercial Bond Program was a highly successful program.

The Cultural and Commercial Corridor Bond – approved by City Council in November 2006, was a highly successful funding program that allowed the City of Philadelphia to assist both cultural institutions and small businesses throughout the city with "hard to fund capital projects." This bond was issued by the Philadelphia Authority for Industrial Development (PAID) on behalf of the City of Philadelphia. The Cultural and Commercial Corridor Bond was not a City-issued bond.

This program is a product of cooperation and collaboration among Philadelphia City Council, several City departments (such as the Streets Department and Public Property), the Office of the Controller, the Philadelphia Industrial Development Corporation (PIDC), the program's administrator, and the Greater Philadelphia Urban Affairs Coalition (GPUAC), under the leadership of the Department of Commerce including the Offices of Economic Opportunity (OEO) and Neighborhood Economic Development.

Timing of this bond program and its approval and implementation played a large role in how the team carried out our due diligence in the management of the program. The guidelines of the bond dictated that 85% of the allocation had to be spent by December 2009 and we worked toward that end, achieving just over 81% spent by the end of the 2009. A large effort of the Bond Program was to encourage grant recipients to use minority owned enterprises for their projects. We are proud to report that at this time, 97% of the Bond – $133million - has been expended with over 25% of those funds going toward minority and women owned enterprises.

Over two hundred grants were issued. Although the intent of the bond was not job creation, it is worth noting that approximately 1,100 construction jobs were created through this public investment.

The Audit Report is incomplete and misleading in its failure to identify the policies and procedures put into place to safeguard the program's objectives and funding and ensure the goals of improving and enhancing the City's cultural and commercial corridors for the benefit of City residents. The Intergovernmental Agreement between PAID and the City, and not exclusively the Department of Commerce, outlines the program goals and sets forth the ground work to carry out the charge – to grant funds to cultural institutions and small businesses throughout the city "with hard to fund" capital projects.

2) Department of Commerce Response to the Audit Findings

"Commerce's Oversight of Corridor Programs was Inadequate"

It is not clear from the Controller's Audit what would have been an adequate and acceptable number of staff to be monitoring the projects and their progress. Commerce can evidence the daily communication among each other as well as with the grantees, and the documented time that was dedicated to this program. Commerce convened a monthly working group meeting called "Bond Working Group" with all program team members. This group of approximately 12 people included representatives from Commerce, PIDC, the Office of Economic Opportunity, the Greater Philadelphia Urban Affairs Coalition (GPUAC), and Labor Standards. At each monthly meeting, our project tracking matrix was reviewed. The matrix included every single grant and its project information, project status, other funding in the project, minority participation, among others things. This document drove each monthly meeting's discussion, which allowed Commerce to monitor all projects including those with challenges that might require special attention.

"Program Goals and Objectives Were Not Clearly Defined and Measured"

- The report quotes the purpose of the bonds was to finance the costs of cultural institution projects and commercial corridor projects. This was accomplished.

- New Freedom Theatre (NFT) controls were, in fact, in place. As stated in the Audit, "As a result [of Department of Commerce controls and conditions on the grant], a second phase of the grant totaling approximately $800,000 was not awarded to the theater". The Department of Commerce would not authorize the remaining $800,000 of the grant to NFT because the grant recipient could not show that it had cleared the debt at the time that it was seeking the remaining grant allocation. We determined that due to our prior efforts to assist the NFT with debt pay-off relief, any additional monies would require proof of a clear record, which NFT did not provide.

"Proper Safeguards against Misuse of Funds Were Not Established"

- The Report questions Commerce's judgment in funding The Merchants Fund to create and administer the ReStore Retail Incentive Grant (RIG) Program because the Director of The Merchants Fund is its sole employee. It does not reference that The Merchants Fund has been in existence since 1854 and is governed by a 12-person board of managers. This is a well-run organization with an exemplary reputation. Despite the finding, the report states, "our review found no errors or improprieties".

  The RIG was created to be a tool for organizations to attract businesses to their neighborhoods. Therefore, both The Merchants Fund and the Department of Commerce publicized the program through extensive email blasts, which contained all the targeted community based organizations. There was no need to use program funds to purchase newspaper and radio advertising as recommended in the report.

  The final note in this section states that the Controller is troubled by a specific award that was made to fulfill a political obligation. The recommendation to refrain from that type of decision making is noted. However, as the report goes on to state "[this specific] project was not completed" and "the grant was never provided". Commerce is actively working with The Merchants Fund to determine a course for re-granting the remaining funds.

- The report recommends that Commerce programs should not have allowed The Reinvestment Fund to issue forgivable loans through the Gap Financing Loan Pool. Forgivable loans are a standard economic development tool when necessary to enable projects to proceed when such assistance will generate jobs, and public benefits, such as a neighborhood supermarket. This is widely acceptable practice and is more cautious and secure development tool than a traditional grant as it holds the recipients to certain milestones in order to be "forgiven".

- The report misrepresents the Streetscape program's process for selecting architectural firms and implies that it was not fair or competitive. Although, it recognizes that "because the corridor bonds were issued by PAID, the Department of Commerce was not required to follow city bidding procedures in selecting the architectural firms". It is true that bids for each individual project were not solicited because of the priority placed on completing the projects. However, a formal RFQ process was publicly advertised, a briefing was held, eight submissions with bids (based on 8 generic corridors) were received and reviewed for the lowest and responsible respondents. A selection committee, that included Commerce, Streets, PIDC, and OEO, short-listed four respondents and then asked for bids based on actual corridors that had since been identified. Then, upon review of those bids, three firms were selected.

"Records Documenting Monitoring Of Project Expenditures Not Maintained"

- The report erroneously states that there was no evidence of project monitoring. It incorrectly suggests that the Department of Commerce was not paying attention to the program. As noted above, there was continual communication and monitoring of projects with one example being the project tracking matrix. GPUAC conducted random site visits as part of their workforce monitoring requirements, which was used as a conduit to alert the team to any issues that were observed with the project. Furthermore, for the majority of the larger projects, the bond grants were leveraged by State Redevelopment Assistance Capital Program funding, which requires PIDC staff to conduct periodic site visits. In addition to PIDC's periodic site visits, State consultants are required to issue reports on each visit. It was determined that this would provide adequate coverage to ensure that projects were being properly managed.

  It shall also be noted that the Office of the Controller performed occasional site visits as well.

"Support for Bond Expenditures Not Always Properly Scrutinized"

- Perhaps the single most important fact that the Audit Report omits is that **each and every** payment request **required** the Office of the Controller's approval. If at any time a payment was rejected, which did occasionally occur, the Bond Team would be required to submit further documentation to receive the Office of the Controller's approval. Even in the example provided in the report, the Office of the Controller "noted no discrepancies between the totals billed and the supporting detail that was hidden [in the submitted invoices]." To date, PIDC has processed 1,578 pay requests across the 200 grants issued. In the few instances of a rejected payment, Commerce adhered to the Office of the Controller's direction.

3) The Controller's method of conducting and sharing this audit was unprofessional and discourteous.

The Department of Commerce was notified of the performance audit and hosted a kick off meeting on July 13, 2011. To help expedite the review process, we instructed all team members to be available to the Office of the Controller. Understanding that the audit would last an estimated six weeks, provisions were made to provide work stations for auditors at both Commerce and PIDC offices in order to have full access to staff and records.

All requests for information by the Office of the Controller were provided promptly to allow the audit team to determine if onsite visits were necessary. Following several months with no communication from the Office of the Controller, on December 13, 2011 Commerce was notified by email that the audit was being suspended. Commerce was notified on April 3, 2012 that the audit was revived and that the report would be shared in May 2012. Again, several months transpired without further communication.

In August 2012 Commerce was informed from sources outside the government that copies of a draft audit report had been provided. The Office of the Controller shared a copy of with a draft report on November 5, 2012, dated September 12, 2012. Upon receiving another revised draft report on November 6, Commerce was instructed by the Office of the Controller to provide our response by noon on November 9, 2012 – as this response accomplishes.

Finally, though the headings and tone of the report infer accusations of poor handling of funds, a statement of actual misuse of funds is not to be found anywhere in the report.

Sincerely,

Alan Greenberger, FAIA
Deputy Mayor for Economic Development
and Director of Commerce

cc: Honorable Michael A. Nutter, Mayor
Honorable Darrell L. Clarke, President
and Honorable Members of City Council
Members of the Mayor's Cabinet

Government Auditing Standards require auditors to evaluate the validity of management's comments when they are inconsistent or in conflict with the findings, conclusions, or recommendations of the report. Overall, we believe management's comments about this report suggest it neither fully comprehended the objectives, scope, and methodology of the review nor understood the nature of the findings and recommendations. Moreover, it did not understand the scope of approval process with respect to the City Controller's Office pre-audit function of the program's disbursements.

Objectives, Scope, and Methodology of Review

Limited time constraints and resources frequently impact the selection of audit projects, as well as the development of objectives, scope, and the methods used when reviewing a particular program or audit subject. These limitations, together with an initial survey, commonly lead auditors to direct their efforts to areas of a program that tend to be the most vulnerable and in need of improvement. Because the Commerce Department had primary oversight responsibility for the Cultural and Commercial Corridors Program, and because our initial survey suggested that procedures to ensure appropriate spending and the most effective use of bond proceeds may not have been in place and operating, we chose to focus on these particular aspects of the program.

Additionally, it is readily apparent that the Commerce Department misunderstood the role of the City Controller's Office in approving payments under the program. As the "independent auditor" for the City of Philadelphia, we carry out our auditing duties in both a pre-audit and post-audit capacity. The pre-audit examination of expenditures serves merely to ensure that funds are available to finance the expenditure and that the intended disbursement appears to be appropriately supported, reasonable, and meets the intent of legislation authorizing the expenditures. This pre-audit examination by the City Controller's Office does not alter the responsibility of city agencies to design and implement procedures that help ensure proper spending of taxpayer dollars. In its post-audit capacity, the City Controller’s Office work is much broader and can involve any number of audit objectives designed to reach a conclusion about a particular aspect of a program’s procedures or operations, including how economical, efficient, and / or effective the program is being run.

With respect to our method of conducting and sharing the audit, which the Commerce Department labeled as "unprofessional and discourteous," the written response to this report was the first notification of the department's ill sentiment regarding our work. As you know, prior to the release of this report, a preliminary draft of the report had been obtained by an unauthorized third party. We took aggressive action to ensure that the Commerce Department received a final draft, had an opportunity to respond at an exit conference held on November 6, 2012, and to provide a written response, which has been included in the final report for release. We take every measure possible to ensure city agencies have an opportunity to respond and participate in the audit process.

Nature of the Findings and Recommendations

In its response, the Commerce Department asserts that the City Controller's Office did not provide a comprehensive review of the program and declares that it will present *"...a full picture of the program and its accomplishments to date."* The department indicates that the Cultural and Commercial Corridors Program was highly successful because it assisted *"...both cultural institutions and small businesses throughout the city with 'hard to fund capital projects.'"* Did the Program provide cultural institutions and small businesses throughout the city with "hard to fund capital projects"? Our work suggested it did. Did these projects *"...improve and enhance the city's cultural and commercial corridors for the benefit of city residents...."* as was the objective of the program according to legislation authorizing issuance of the bonds and the bond indentures themselves? We were unable to ascertain the answer to this question.

As the City Controller's Office found and reported, the Commerce Department's oversight of the Cultural and Commercial Corridors Program was frequently not apparent. Although the Commerce Department asserts the program was successful, it could not provide us with evidence that it actively measured program goals and objectives. It could not demonstrate, for instance, that after it had provided the NFT with $2.2 million that it was monitoring the continued viability of the theater, as quantitatively measured by increased ticket sales and / or increased program enrollment, for example. Likewise with other projects it funded along the corridors, the Commerce Department did not measure indicators such as sales increases or jobs created. Nor did it keep data on new business starts or the number of refurbished vacant properties, or even the change in crime within the corridors. While throughout the audit, the Commerce Department asserted it kept specific data or performed certain procedures, it could not provide us with evidence to substantiate the data was kept or the procedures were being completed.