

Chesapeake VIRGINIA

ECONOMIC DEVELOPMENT PERFORMANCE AUDIT REPORT



SEPTEMBER 28, 2021

AUDIT SERVICES DEPARTMENT
CITY OF CHESAPEAKE, VIRGINIA

THIS PAGE IS INTENTIONALLY BLANK

Table of Contents	<u>Page</u>
<i>“Promoting Accountability and Integrity in City Operations”</i>	1
Transmittal Letter	2
<i>Acknowledgements</i>	4
AUDIT HIGHLIGHTS.....	5
Executive Summary	6
ECONOMIC DEVELOPMENT COMPREHENSIVE REPORT	13
A. Objectives, Scope, and Methodology	13
B. Performance Information.....	16
1. Economic Development - Mission	16
2. CARES Money for Small Businesses	16
3. Greenbrier and South Norfolk Tax Increment Financing Districts (TIF’s).	17
4. Services and Economic Development Investment Program (EDIP)	17
C. Economic Development – EDIP and Operational Issues	20
1. Memorandum of Understanding	20
2. Development Agreements Updating	21
3. Resolutions and Worksheet Calculations.....	23
4. Development Agreements – Signed Originals and Notary Issues.....	25
5. EDIP Grant Payment Issue	27
6. Segregation of Duties	28
7. Petty Cash and Travel Funds	30
APPENDIX A: RESPONSE FROM ECONOMIC DEVELOPMENT OFFICIALS	33

THIS PAGE IS INTENTIONALLY BLANK



Economic Development Performance Audit Issued September 28, 2021

“Promoting Accountability and Integrity in City Operations”

Chesapeake City Council

Honorable Mayor Rick W. West	Robert C. Ike, Jr., Council Member
Dr. John de Triquet, Vice Mayor	S.Z. “Debbie” Ritter, Council Member
R. Stephen Best, Sr., Council Member	Susan R. Vitale, Council Member
Don J. Carey III, Council Member	Dr. Ella Ward, Council Member
Matthew R. “Matt” Hamel, Council Member	

Audit Committee Members

S.Z. “Debbie” Ritter, Audit Committee Chair
Matthew R. “Matt” Hamel, Audit Committee Member
Patrick E. Corbin, CPA, Audit Committee Citizen Member

Audit Services Department

Darren M. Padilla, CIA, CRMA, Acting City Auditor
Anthony J. Markun, CFE, CFSA, CBA, CRMA, CICA, Deputy City Auditor
E. Keith Jeter, CICA, Performance Auditor 2
Adriane Fisher, CICA, Audit Specialist

Audit Services Department
306 Cedar Road
Chesapeake, Virginia
23322
(757) 382-8511
Fax (757) 382-8860

September 28, 2021

The Honorable Mayor Rick W. West and
Members of the City Council
City of Chesapeake
City Hall – 6th Floor
Chesapeake, Virginia 23322

Dear Mayor West and Members of the City Council,

We have completed our review of the Chesapeake Department of Economic Development (ED) for December 1, 2020 – May 31, 2021. Our review was conducted for the purpose of determining whether the ED was providing services in an economical, efficient, and effective manner, whether its goals and objectives were being achieved, and whether it was complying with applicable City and Department procedures related to their Economic Development Incentive Program, City Resolutions, Development Agreements, Petty/Travel Cash, and general management oversight, including segregation of duties.

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 conclusion 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.

The Department provided essential services for the City of Chesapeake (City) primarily the recruitment of high-quality businesses to the City. Coupled with that was their focus on retaining and helping expand existing businesses and industries. Their goal was to expand and create a diverse and stable tax base and increase overall tax revenue, by increasing business investment and job creation. ED partnered with various state and local organizations such as the Hampton Roads Economic Development Alliance (HREDA) and the Virginia Economic Development Partnership (VEDP) to achieve these goals. These partnerships and the development and implementation of various programs encouraged industries and businesses to locate, and expand, within the City. The Economic Development Central Office Function also performed staffing functions for the Economic Development Authority (EDA) and Economic Development Advisory Committee and provided staff oversight for the Greenbrier and South Norfolk TIF districts. ED also served as liaison between the industrial and business communities and the City.

For Fiscal Year (FY) 2020-2021, the Department had an operating budget of almost \$4 million and an authorized compliment of 11 personnel. The largest item in the ED budget was over \$1.4 million (35.98%) for various incentive programs. The next largest item in the

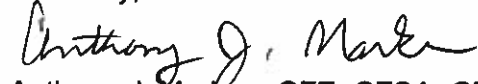
budget was a little under \$1.2 million (29.81%) for salaries and benefits.

To conduct this audit, we reviewed and evaluated City and Department policies and procedures, and operations documents and reports, both internal and external. We interviewed department management and staff. We examined the Department's Economic Development Incentive Grant Program (EDIP) in detail.

Based on our review, we determined the Department had accomplished its overall mission of attracting and retaining a diverse and stable business base. However, we did identify several areas of concern that needed to be addressed. Those areas included the lack of a formal memorandum of understanding, between the City and EDA, the need to update and modify the development agreements, compliance issues with City resolutions, calculation issues with a grant spreadsheet, issues maintaining the original, signed, development agreements in a central location as well as the accuracy of the notaries being used. There were also concerns with the timely payment of grants, segregation of duties, and petty/travel cash handling.

This report, in draft, was provided to the Department officials for review and response. Their comments have been considered in the preparation of this report. These comments have been included in the Managerial Summary, the Audit Report, and Appendix A. Department management and staff, especially the management analyst, were very helpful throughout the course of this audit. We appreciated their courtesy and cooperation on this assignment.

Sincerely,



Anthony J. Markun, CFE, CFSA, CBA, CRMA, CICA
Deputy City Auditor
City of Chesapeake, Virginia

C: Christopher M. Price, City Manager
Steven C. Wright, Economic Development Director



Economic Development Performance Audit

Acknowledgements

We would like to thank Steven Wright, Director, Ben White, Deputy Director, and Constantia Matthews, Management Analyst and staff of the Economic Development department for their full cooperation and assistance throughout this audit during the COVID pandemic. Our hope is that this audit serves as a tool to provide the City Council, Economic Development, and City leadership with the necessary insight for continuous improvement of the administrative operating conditions of the Economic Development department.

Additional thanks are extended to the City's Legal, Finance and Budget Departments, as those departments were also instrumental in providing information necessary to conduct this performance audit.

It is also appropriate to thank the City Manager and his staff, Mayor and Members of the City Council, and the Members of the Audit Committee for their interest and support in planning and conducting the independent internal audit activities of the City.

Finally, I want to thank and recognize Audit Services department staff. Special thanks to Mark Crist and Keith Jeter for their contributions, assistance, and support throughout this audit.

Anthony J. Markun, CFE, CFSA, CBA, CRMA, CICA
Deputy City Auditor

AUDIT HIGHLIGHTS

September 28, 2021

Audit Report No. 131

WHY WE DID THIS AUDIT

An audit of Economic Development (ED) was included on the City Council-approved fiscal year 2020/21 Audit Plan. The audit objective was to review the Economic Development Incentive Program (EDIP) program and to ensure that controls were in place to assure the Economic Development Authority (EDA), and the City, that funds distributed for the EDIP are adequately accounted for and properly recorded.

BACKGROUND

In 2020, Economic Development changed their business model to address the City's response to the COVID pandemic. In addition to carrying out its core mission, Economic Development assignments expanded to coordinate and issue checks to businesses for the Small Business COVID-19 Recovery Grants program.

EDA holds a unique relationship with the Economic Development Department. Administrative and financial EDA processes are performed by City employees of the Economic Development Department. Those EDA administrative processes include cash handling, bookkeeping, reconciliements, and overall management of the ED EDIP Grant Award program.

WHAT WE FOUND

Favorable Observations Noted:

- ED was actively marketing Chesapeake as an ideal location for business with easy access to regional transportation hubs and access to one of the largest commercial shipping ports in the world.
- ED was successful in coordinating and issuing checks to businesses for the Small Business COVID-19 Recovery Grants program for Chesapeake to reimburse business expenses incurred on or after 3/1/2020; processing four rounds of grants with 88% of businesses that applied for \$5.6M available.
- ED was managing the Greenbrier and South Norfolk TIFs created to provide funding for public infrastructure projects to help attract private investment to the City.
- ED partnered with other state and regional organizations such as Hampton Roads Economic Development Alliance (HREDA) and Virginia Economic Development Partnership (VEDP) to provide a wide assortment of incentives to businesses to bring them into Chesapeake.

Opportunities for improvement:

EDIP Processes Reviewed	Description of Issues	Management Action
Memorandum of Understanding	Economic Development (ED) was providing various administrative/financial services for the Economic Development Authority (EDA). Economic Development (ED) did not have a Memorandum of Understanding (MOU) with the EDA that addressed which entity had job and oversight responsibilities for the various services provided to the EDA.	Open Item
Development Agreement Modifications	Development Agreements for EDIP grants need to be reviewed and amended to make clear that it is the grant recipient's responsibility to notify ED/EDA when events occur that affect the terms of the Development Agreement. The result was a payment for \$100,000 being released by the City, and deposited to the EDA, in preparation for awarding. The business failed to report that it had been sold after the grant was awarded. The new owners were not aware of the EDIP agreement and did not want to accept the payment. City Finance, EDA, and ED are in the process of returning the money to the City.	Pending City Action
Resolutions and adherence to them	Resolution amendments, approved by City Council, to the Economic Development Investment Grant Program, omitted tables that were referenced in the resolution. The worksheet that ED/EDA used to determine the maximum amount of funds that were available for the Economic Development Investment Grant Program (EDIP) to a company, was not calculated in accordance with the Investment Grant Resolution dated July 12, 2016.	Open Items
Contract Administration	Official copies of development agreements (DAs) were found not to be signed, accurately notarized, properly dated or kept in a central location.	Open Item
Timeliness of EDIP Payments	The first EDIP Grant payments were not always processed in accordance with the development agreements (DAs).	Open Item
Segregation of Duties	Economic Development (ED) maintains the financial records for the Economic Development Authority (EDA). We found that segregation of duties and compensating controls needed to be improved. In addition, there were no documented procedures in place for the disbursement process.	Open Item
Compliance with Petty/Travel cash handling guidelines	Documented procedures for petty/travel cash funds had not been developed, written, and implemented. Sufficient internal controls were not in place to safeguard these assets nor was Economic Development following Finance Department's citywide Petty/Travel Cash procedures.	Corrective Measures Taken (The Travel Fund was returned to the City.)

Executive Summary

We have completed our audit of the Chesapeake Department of Economic Development (ED) for December 1, 2020 – May 31, 2021. Our audit was conducted for the purpose of determining the effectiveness and efficiency of their Economic Development Incentive Program.

The Department provided essential services for the City of Chesapeake (City) primarily the recruitment of high-quality businesses to the City. Coupled with that was their focus on retaining and helping expand existing businesses and industries. Their goal was to expand and create a diverse and stable tax base and increase overall tax revenue, by increasing business investment and job creation. ED partnered with various state and local organizations such as the Hampton Roads Economic Development Alliance (HREDA) and the Virginia Economic Development Partnership (VEDP) to achieve these goals. We examined the Department’s Economic Development Incentive Grant Program (EDIP) in detail.

As part of its’ efforts to assist businesses affected by the pandemic congress passed the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES act. This act appropriated money for various programs to help small businesses throughout the country that were affected by the pandemic. As part of this assistance effort ED was tasked with coordinating the **Small Business COVID-19 Recovery Grants** program for Chesapeake. These grants were for reimbursable business expenses incurred on or after March 1, 2020. The ED reviewed applications from Chesapeake businesses that stayed open during the pandemic and attempted to retain their staff. The grant amounts were up to \$12,500.00 for businesses with 50 employees or less. The ED processed four rounds of grants with 88% percent of those businesses applying for and receiving a portion of the over \$5.6 million given away. Totals from round 4 were still under review. With each new round ED adjusted the parameters of the grants to encourage increased applications of qualifying businesses.

**Table 1
CARES Act Grant Program**

Round	Number of Applications	Number Approved	% Approved	Total of Grants
1	61	15	24.59%	\$50,000.00
2	279	252	90.32%	\$2,352,630.33
3	128	105	82.03%	\$1,042,498.00
4	390	384	98.46%	\$2,161,551.00
Totals	858	756	88.11%	\$5,606,679.33

This information was supplied by the Economic Development Department and was not audited.

C. Economic Development – EDIP and Operational Issues

We reviewed the ED/EDA EDIP Investment Grant Program, overall structure and operating practices and determined that although they were meeting their expectations there are still areas that could be improved. These areas included the ED/EDA not having a memorandum of understanding, need for development agreement modifications, not having accurate City resolutions, and not adhering to those resolutions. Issues were found involving maintaining the original, signed, DAs in a central location as well as the accuracy of the notaries being used. Also, the Department needed to improve the timeliness of EDIP payments, their segregation of duties and petty/travel cash handling processes.

The following findings were identified as opportunities for improvement:

1. Memorandum of Understanding

Finding – Economic Development (ED) provided various administrative/financial services for the Economic Development Authority (EDA). Economic Development (ED) did not have a Memorandum of Understanding (MOU) with the EDA that addressed which entity had job and oversight responsibilities for the various services provided to the EDA.

We found that ED did not have an MOU that addressed the rights, duties, obligations, terms, and intentions of the parties. In addition, we found that job and oversight responsibilities for services provided to the EDA were not documented as to which entity had oversight responsibility for ED services provided.

Recommendation – The agreement between the ED and the EDA for providing various administrative/financial services should be reduced to writing using an MOU to capture the rights, duties, obligations, terms, and intentions of all the parties involved, and identify remedies for breach of the agreement.

Response: Though there have been no issues, concerns or disputes with the Economic Development Department employees performing various duties and functions as staff to the Economic Development Authority since at least 1998 (earliest start date of current staff members) and likely since the Economic Development Authority/Industrial Development Authority inception in 1966, we do not dispute the finding for the need of an MOU between the EDA and Department of Economic Development/City of Chesapeake. We have engaged the City Attorney in creating an MOU for City Council and Economic Development Authority consideration, which will capture the rights, duties, obligations, terms, of the relationship between the City of Chesapeake, Economic Development Staff, and the EDA.

2. Development Agreements Updating

Finding – Development Agreement for Economic Development Investment Grant Program needs to be reviewed and amended to make clear that it is the grant recipient's responsibility to notify ED/EDA when events occur that affect the terms

of the Development Agreement.

In 2018, Project Cold Storage, applied to the Economic Development Authority (“EDA”) for a grant under the Economic Development Incentive Grant program. On December 11, 2018, City Council adopted a resolution authorizing a grant award, and appropriated \$300,000 to be transferred to the ED/EDA for the grant.

Project Cold Storage was acquired by Company A, in March 2019 (the sale closed in May 2019).

The final Certificate of Occupancy (C.O.) for Project Cold Storage facility expansion was issued in November 2019. The ED/EDA was not aware at that time that Company A had acquired Project Cold Storage. When the ED/EDA became aware of the issuance of the final C.O., a check for \$100,000 representing payment of the first installment of the grant to Project Cold Storage was cut, but Company A returned the check, saying that they were not familiar with the existence of the grant and not interested in pursuing it. The EDA and ED staff were in the process of working with Finance to return the \$100,000 funds to the City.

The ED/EDA had not experienced this situation with prior grants. There was some lag time between the date of issuance of the final C.O., and the ED/EDA becoming aware that the C.O. had been issued. Project Cold Storage did not notify the ED/EDA that they were being acquired by Company A. In addition, our review of the Development Agreement revealed that the agreement did not articulate what information a company had to provide the ED/EDA (i. e. business being sold, permit number, Copy of C.O., Investment Grant Program Worksheet completed before the second and third payments will be made).

Recommendation – We recommend that consideration be given to review and amend the Development Agreement, to make clear that it is the grant recipients responsibility to notify the ED/EDA of any events and/or changes to their circumstances that may impact the recipient’s performance under the Development Agreement. Also, the Economic Development Incentive Grant program policy may also need to be reviewed and amended to clarify the parties’ reporting responsibilities. (The \$100,000 was returned to the City during our audit.)

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters as they are responsible for crafting of Development Agreements. To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

3. Resolutions and Worksheet Calculations

Finding – Resolution amendments, approved by City Council, to the Economic Development Investment Grant Program, omitted tables that were referenced in the resolution.

The worksheet that ED/EDA used to determine the maximum amount of funds that were available for the Economic Development Investment Grant Program (EDIP) to a company, was not calculated in accordance with the Investment Grant Resolution dated July 12, 2016.

Our review of the ED amendment adopted 7/14/09 found that it did not include three of the eight referenced tables. Review of the ED amendment adopted 7/12/16 found that it did not include the only table referenced in the amended resolution.

The EDIP Grant amounts were calculated using a point system. This point system assigned a point value for each of these seven attributes: jobs created, salaries, real estate investment, machinery and tools investment, business personal property investment, infrastructure improvements, and admissions tax. We found that three of the seven attributes, salary, machinery, and business personal property investments, were not calculated in accordance with the July 12, 2016 resolution amendment.

Recommendation – ED/EDA should ensure that all tables, and other material, referenced in resolutions, are in fact included, prior to them going before the City Council for approval. Develop a monitoring and oversight process for the review of resolutions. Change the Grant Calculation worksheet to reflect the calculation method that is included in the City Council amendment. Process a new amendment to correct the last amendment in order to have the calculations work as the EDA expected.

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the EDIP Resolution so that it is consistent with the Economic Development Department's Grant Calculation Worksheet. The Economic Development Department does not dispute this finding but will defer to the City Attorney and EDA Attorney on crafting of the EDIP Resolutions, with the input and careful review of Economic Development Staff. Economic Development acknowledges there was a minor inconsistency in the Grant Calculation Spreadsheet and has adjusted the calculations accordingly. As a result of the minor inconsistency in the Grant Calculation Spreadsheet, no businesses received grant awards beyond what they were qualified. Neither the City of Chesapeake, nor any grant awardees, were negatively impacted by the Grant Calculation Spreadsheet inconsistency.

To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

4. Development Agreements – Signed Originals and Notary Issues

Finding – Official copies of development agreements (DAs) were found not to be signed, accurately notarized, properly dated or kept in a central location.

Audit Services selected 19 DAs for review. Between the ED/EDA files and those of the City Clerk's office, copies of all the agreements were found. However, not all agreements were found in one area.

Errors [in notarization] included leaving the date of the agreement off the notary stamp, using a wrong date for the agreement, and indicating that the agreement was signed before the date of the agreement.

One of the DAs had a pen and ink change made to the date of the DA without having the change properly initialed and dated by both parties.

Recommendation: Management should consider establishing quality assurance review procedures of DAs to ensure that completed, signed original development agreements are sent to the City Clerk's office as soon as executed.

Response: Economic Development does not dispute the findings. Since this Audit commenced a new staff member has been added to the Department with extensive legal experience and with significant experience as a Notary of Public with knowledge of procedures and guidelines set forth in Virginia Law. This staff member had been added to the Department review process to ensure all Development Agreements are complete, signed and properly notarized prior to being sent to the City Clerk. Economic Development is also investigating the use of digital signature software as an alternative solution to use of a Notary of Public.

5. EDIP Grant Payment Issue

Finding – The first EDIP Grant payments were not always processed in accordance with the development agreements (DAs).

We randomly selected ten EDIP grant DAs, to determine if the first payments were paid in accordance with the DAs. DA's, selected for review, required that the first EDIP payment be made 60 days after the issuance of a certificate of occupancy. Our review of the DAs revealed that all had certificates of occupancy that were dated between 6/9/2017 and 1/11/2021. Of the ten agreements reviewed, 5 (50.0%) were paid as required, while 5 (50.0%) were paid after the agreed payment period had elapsed.

Recommendation – Management should ensure that all EDIP payments are paid in accordance with the DAs. In addition, management should develop and implement a monitoring process to ensure payments are made timely.

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters such as the crafting of Development Agreements.

6. Segregation of Duties

Finding – Economic Development (ED) maintains the financial records for the Economic Development Authority (EDA). We found that segregation of duties and compensating controls needed to be improved. In addition, there were no documented procedures in place for the disbursement process.

Our review of the financial records determined that an ED employee was responsible for maintaining the EDA financial records in Quick Books. We found that documented procedures had not been developed for the disbursement process.

One individual performs [multiple] functions which diminishes segregation of duties.

In addition, we found [multiple] concerns related to compensating controls.

Recommendation: We recommend that documented procedures be established to ensure segregation of duties and compensating controls are in place. In addition, a monitoring process should be established to ensure internal controls are in place and functioning as designed.

Response: The Economic Development Department does not dispute the findings and has address the following items as described above:

- *All check numbers should be entered into Quick Books.*
 - All checks are entered into Quick Books, including voided checks.
- *If issued checks have forged signatures, the Bank does not verify that issued checks contain only authorized signatures.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *The numerical sequence of issued unissued, voided, and missing checks should be verified by an independent person on a periodic basis.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *Incorporate use of a missing checks report from Quick Books as part of the reconciliation review process.*
 - Missing checks report is printed and reviewed by the Executive Secretary of the EDA on a monthly basis.

- *Consider requesting the bank to send EDA the front and backs of checks so that the endorsements can be reviewed.*
 - The front of checks are provided monthly as part of the bank statements and backs of checks are now being requested.
- *Fulton unissued check stock should be destroyed in the presence of two persons and the verification should document the beginning and ending numbers and the signatures and date of the two persons who verified the destruction of the checks.*
 - Closed Fulton Bank account check stock have been destroyed and verified by two people who signed and dated a statement confirming destruction.
- *Develop a backup plan for this function in the case this person is out of the office for an extended period.*
 - The EDA is contracting for Accounting and Audit Services and will include as part of these, back up accounting services in the event of an extended leave for Economic Development Staff member who performs monthly accounting functions for the EDA.

The Economic Development Department has procedures in place that include the Executive Secretary of the EDA to providing monthly review and oversight of the financial duties and functions performed by the Economic Development Staff on behalf of the EDA

7. Petty Cash and Travel Funds

Finding – Documented procedures for petty/travel cash funds had not been developed, written, and implemented. Sufficient internal controls were not in place to safeguard these assets nor was Economic Development following Finance Department’s citywide Petty/Travel Cash procedures.

We evaluated the internal control process for petty/travel cash funds and determined that internal controls were not in place and assets were not safeguarded. We found [multiple] control weaknesses that need to be addressed.

The travel fund was last used in 2018, and the petty cash fund was last used in April 2019. **The \$2000 travel fund was returned to Finance during our audit.**

Recommendation – ED should develop and document petty/travel cash fund procedures so that cash funds are safeguarded. In addition, ED should develop a monitoring process to ensure adherence to petty/travel funds control procedures.

Response: Economic Development does not dispute the findings and as such has established and is following procedures requiring monthly counts with accompanying documentation (which exceeds City requirements of quarterly counts), and receipts for replenishment handled on a monthly basis. Additionally, Economic Development has eliminated the \$2,000 Travel Fund because it was used sparingly and not at all since the start of the Pandemic.



ECONOMIC DEVELOPMENT COMPREHENSIVE REPORT

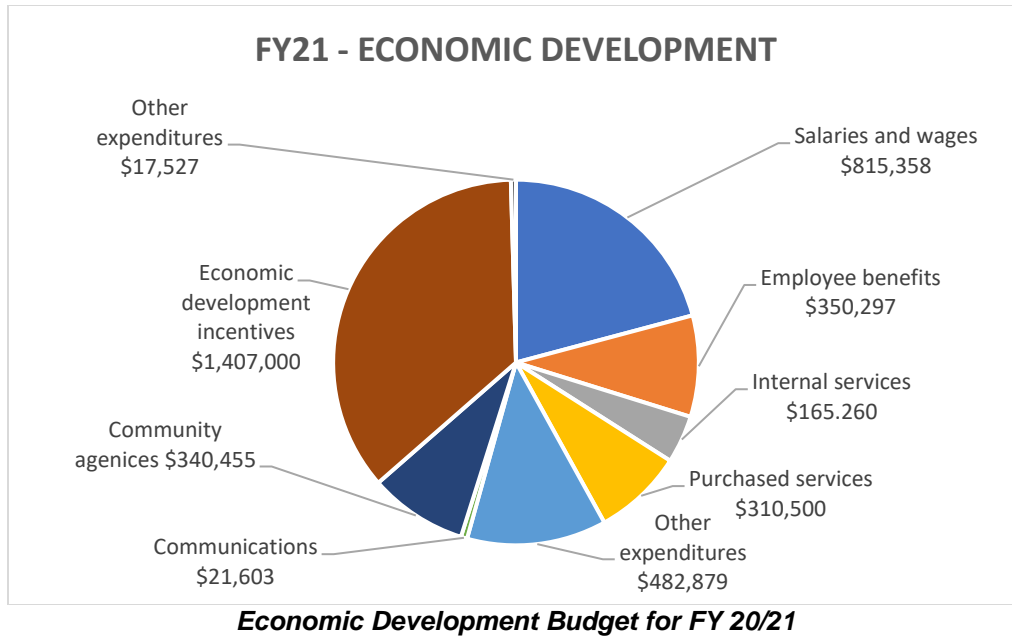
A. Objectives, Scope, and Methodology

We have completed our review of the Chesapeake Department of Economic Development (ED) for December 1, 2020 – May 31, 2021. Our review was conducted for the purpose of determining whether the ED was providing services in an economical, efficient, and effective manner, whether its goals and objectives were being achieved, and whether it was complying with applicable City and Department procedures related to their Economic Development Incentive Program, Memorandums of Understanding, City Resolutions, Development Agreements, general management oversight, including segregation of duties, and Petty/Travel Cash.

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 conclusion 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.

The Department provided essential services for the City of Chesapeake (City) primarily the recruitment of high-quality businesses to the City. Coupled with that was their focus on retaining and helping expand existing businesses and industries. Their goal was to expand and create a diverse and stable tax base and increase overall tax revenue, by increasing business investment and job creation. ED partnered with various state and local organizations such as the Hampton Roads Economic Development Alliance (HREDA) and the Virginia Economic Development Partnership (VEDP) to achieve these goals. These partnerships and the development and implementation of various programs encouraged industries and businesses to locate, and expand, within the City. The Economic Development Central Office Function also performed staffing functions for the Economic Development Authority (EDA) and Economic Development Advisory Committee and provided staff oversight for the Greenbrier and South Norfolk TIF districts. ED also served as liaison between the industrial and business communities and the City.

For Fiscal Year (FY) 2020-2021, the Department had an operating budget of almost \$4 million and an authorized compliment of 11 personnel. The largest item in the ED budget was over \$1.4 million (35.98%) for various incentive programs. The next largest item in the budget was a little under \$1.2 million (29.81%) for salaries and benefits.



To conduct this audit, we reviewed and evaluated City and Department policies and procedures, and operations documents and reports, both internal and external. We interviewed department management and staff. We examined the Department's Economic Development Incentive Grant Program (EDIP) in detail.

Major Observations and Conclusions

Based on our review, we determined the Department had accomplished its overall mission of attracting and retaining a diverse and stable business base. However, we did identify several areas of concern that needed to be addressed. Those areas included the lack of a formal memorandum of understanding, between the ED and EDA, the need to update and modify the development agreements, compliance issues with City resolutions, calculation issues with a grant spreadsheet, issues maintaining the original, signed, development agreements in a central location as well as the accuracy of the notaries being used. There were also concerns with the timely payment of grants, segregation of duties, and petty/travel cash handling.

This report, in draft, was provided to the Department officials for review and response. Their comments have been considered in the preparation of this report. These comments have been included in the Managerial Summary, the Audit Report, and Appendix A. Department management and staff, especially the management analyst, were very helpful throughout the course of this audit. We appreciated their courtesy and cooperation on this assignment.

Methodology

To conduct this audit, we reviewed various aspects of the EDIP that included expenses, individual companies' development agreements, incentive grant calculation sheets and methodologies, and City resolutions for compliance with City policies and procedures. We conducted interviews with department management and staff. We also did an overall assessment of the Department's organizational structure and reviewed operational practices and procedures, including cash handling, throughout the department.

This audit presented some obstacles not normally found in audits. These obstacles effected both ED and Audit Services and were the result of having conducted the audit during a worldwide pandemic. During most of 2020 and into early 2021 ED staff operated totally or occasionally by teleworking. This resulted in months of ED operations being conducted from remote locations and not in the ED offices. The remote operations resulted in ED having to change how business was conducted, specifically the increase in the use of electronic documentation and a disruption of normal ED processes and workflows. Also, as part of the pandemic relief, ED was tasked with managing the CARES grant programs to provide relief for Chesapeake businesses. This consumed a large amount of the ED staff's time. Audit services appreciated the efforts of the ED management, and staff, in accommodating this audit during the pandemic restrictions.

B. Performance Information

Good schools, safe streets, well-paying jobs, and low taxes were some of the qualities individuals and families looked for in a city when they were considering where to call home. These were also some of the same qualities' businesses looked for in a city when they were considering where to locate or expand. Assisting businesses to locate, or expand, in Chesapeake was the job of Economic Development. Whether it was an international company like Yupo, or a Fortune 500 corporation like Dollar Tree, Economic Development had the tools and the capabilities to help businesses make Chesapeake their home. High value, quality businesses that resided in the City had a positive impact on the tax base. This in turn helped to keep residential taxes low, provided money for good schools, safe streets, and provided well-paying jobs for the over 240,000 residents of the City. Economic Development was a key lynchpin in the City's efforts to maintain Chesapeake as a city that businesses, and families, wanted to move to and make their home.

1. Economic Development - Mission

Economic Development was tasked with bringing in new business from targeted industries and retaining existing businesses already in the City. The ED helped businesses find the right location among the City of Chesapeake's more than 14 million square feet of retail space, almost 18 million square feet of industrial space and almost 5.5 million square feet of office space. The ED marketed a City with an ideal location for businesses. The City utilized a regional transportation hub consisting of highways, airports, rail service, and access to one of the largest commercial shipping ports in the world. In addition, the City was located within highway hours of almost two-thirds of the national population. Ready access to a diverse and educated workforces only enhanced the tools that the ED used to attract and retain businesses.

In FY 2018-2019, the ED helped bring in over \$242 million of additional investment in businesses in Chesapeake. Several major projects were announced or completed during FY 2019-2020. These included the proposed \$10 million expansion of Sumimoto Machinery Corporation of America, and the over \$2 million expansion of Big Ugly Brewing Company, LLC. Both projects and many more like them would bring jobs and investment to the City.

2. CARES Money for Small Businesses

As part of its' efforts to assist businesses affected by the pandemic congress passed the Coronavirus Aid, Relief, and Economic Security Act, also known as the CARES act. This act appropriated money for various programs to help small businesses throughout the country that were affected by the pandemic. As part of this assistance effort ED was tasked with coordinating the Small Business COVID-19 Recovery Grants program for Chesapeake. These grants were for reimbursable business expenses incurred on or after March 1, 2020. The ED reviewed applications from Chesapeake businesses that stayed open during the pandemic and attempted to retain their staff. The grant amounts were up to \$12,500.00 for businesses with 50 employees or less. The ED processed four rounds of grants with 88%

percent of those businesses applying for and receiving a portion of the over \$5.6 million given away. Totals from round 4 were still under review. With each new round ED adjusted the parameters of the grants to encourage increased applications of qualifying businesses.

**Table 1
CARES Act Grant Program**

Round	Number of Applications	Number Approved	% Approved	Total of Grants
1	61	15	24.59%	\$50,000.00
2	279	252	90.32%	\$2,352,630.33
3	128	105	82.03%	\$1,042,498.00
4	390	384	98.46%	\$2,161,551.00
Totals	858	756	88.11%	\$5,606,679.33

This information was supplied by the Economic Development Department and was not audited.

3. Greenbrier and South Norfolk Tax Increment Financing Districts (TIF's)

As part of its' oversight functions ED managed the two City TIF's. The Greenbrier and South Norfolk TIF's were created to provide funding for public infrastructure projects that were needed to help attract additional private investment to the City, and specifically into the Greenbrier and South Norfolk areas. The Greenbrier TIF was established on January 1, 2005 and the South Norfolk TIF was established on March 22, 2005. Both TIFs are funded by taking tax revenue, over a specified base, from the affected areas and using this money to fund the various projects in those districts.

As projects are designated, a dollar estimate is made of the cost, funding streams are decided upon, and bonds are issued if required. Bonded debt payments are supported by TIF tax revenues, and bond proceeds are placed into the State Non-Arbitrage Program (SNAP) until needed. Projects were managed by an external management firm, McDonough Bolyard Peck (MBP), which filed monthly status updates with the Department. MBP also assisted the City's Public Procurement Office with the selection of vendors necessary for each project.

4. Services and Economic Development Investment Program (EDIP)

As part of its overall mission to attract and retain businesses in the City ED had multiple tools at hand. ED partnered with other state and regional organizations such as Hampton Roads Economic Development Alliance (HREDA) and Virginia Economic Development Partnership (VEDP) to be able to provide a wide assortment of incentives to businesses. Whether tax exemptions or state workforce and investment grants or tax credits, ED tried to find the right fit for each company.

One of the incentives used was the EDIP. This investment grant program generally provided a small incentive to businesses that needed help get their project over the finish line. The application process took into consideration the capital investment, real estate

investment, admissions tax generated, and jobs, and salaries, created. After reviewing the annual tax revenue to be generated, usually over three years, a decision was made, by ED, on whether, or not, to award a grant, usually payable in three installments, to the business. To receive the grant, the proposed project had to be completed in accordance with a signed development agreement.

A review of data provided by ED indicates that only a small percentage of prospective projects became projects. Table 2 shows that of 297 prospects only 78.79% (234/297) became projects. Of that 234 an even smaller percentage, 32.91% (77/234), were won by the City of Chesapeake. A Won project was where the business located or expanded in the City. Of those projects that located or expanded in the City only 9.09% (7/77) offered an EDIP grant.

**Table 2
Chart of Prospects, Project Wins, and Project Losses**

	EDIP Overview - Prospects to EDIP				TOTAL
	Pre-2018*	2018**	2019	2020	
Total Prospects	150	58	61	28	297
Total Projects	144	50	37	3	234
Projects Won	60	12	5	0	77
Projects Lost	71	34	26	4	135
EDIP Offered/Awarded	4	3	0	0	7
% Prospect to Projects	96.00%	86.21%	60.66%	10.71%	78.79%
% Projects to Won	41.67%	24.00%	13.51%	0.00%	32.91%
% Projects to Lost	49.31%	68.00%	70.27%	133.33%	57.69%
% Projects Won that were Offered EDIP	6.67%	25.00%	0.00%	0.00%	9.09%
% Total Projects that were Offered EDIP	2.78%	6.00%	0.00%	0.00%	2.99%
% Total EDIP Grant Awards to Prospects	2.67%	5.17%	0.00%	0.00%	2.36%

It may take Prospect's years to become a project. This chart only reports what happened in each year. There were 22 projects whose won/lost status was not resolved during 2018 – 2020.

Notes/Definitions to Table 2:

"Prospect": Inquiry from Company to come to Chesapeake or expand in Chesapeake.

"Project": Following inquiry, company proceeds with move/expansion and provides Capital Investment and Jobs Numbers.

"Project Won": Company finalizes real estate contract and begins their move/expansion in Chesapeake.

"Project Lost": Company does not move/expand in Chesapeake.

"EDIP Offered/Awarded": Company offered EDIP Grant by ED/EDA

The data moved from one system to the current tracking system. Due to the transfer of data, everything prior to April 1, 2018 is not dated.

*Pre-2018: Everything prior to April 1, 2018

**2018: April 1, 2018 - December 31, 2018

Lost projects are projects that do not relocate or expand to Chesapeake. There were many reasons for Lost projects. Some of the projects were national in scope and were handled by the Commonwealth. These types of projects generally review many sites and may be looking for major concessions that were not possible in Chesapeake. Another reason was that often the project could not be based in Chesapeake due to the absence of product necessary for the project. This lack of product included insufficient land, insufficient land with necessary infrastructure such as roads and sewers, or not the right mix of education and skill diversity. Each project had its' own needs and whether ED won or lost a project in most cases had nothing to do with Economic Development efforts. Table 3 showed the many reasons projects were Lost to the City.

**Table 3
Chart of Reasons for Losses**

REASONS PROJECTS DID NOT RELOCATE/EXPAND IN CHESAPEAKE		
	Total Projects	% of Total Projects
	135	
Cancel	11	8%
Competing Location	25	19%
Council Denied	1	1%
Failed to Qualify	28	21%
Other	6	4%
Project Died	46	34%
Reason Unknown (Blank)	15	11%
Entered in Error	3	2%

Notes/Definitions to Table 3:

"Cancel" - the company has informed us that they wish to cancel their prospect/project.

"Competing Location" - Chesapeake lost the prospect/project to another location.

"Council Denied" - City Council denied the prospect/project.

"Failed to Qualify" - Chesapeake failed to qualify to move forward with a company due to lack of resources. A common example is the lack of infrastructure, or land.

"Other" - Any reason not provided in the options. An example is Project Weekend Warrior, and their "Other" reason is lack of financing to continue with the project.

"Project Died" - No response from the company that made the initial inquiry.

"Reason Unknown (Blank)" - No reason was provided by the company.

"Entered in Error" - Entered into the system in error, or as a test.

In addition to incentives ED offered a wide range of services to businesses that desired to do business in Chesapeake. If ED could not directly assist a company, they had access to various professionals and local services necessary to get the business started or keep the business growing. These professionals could help with local advisory services,

site selection, and business certifications.

C. Economic Development – EDIP and Operational Issues

We reviewed the ED/EDA EDIP Investment Grant Program, overall structure and operating practices and determined that although they were meeting their expectations there are still areas that could be improved. These areas included the ED/EDA not having a memorandum of understanding, need for development agreement modifications, not having accurate City resolutions, and not adhering to those resolutions. Issues were found involving maintaining the original, signed, DAs in a central location as well as the accuracy of the notaries being used. Also, the Department needed to improve the timeliness of EDIP payments, their segregation of duties and petty/travel cash handling processes.

1. Memorandum of Understanding

Finding – Economic Development (ED) provided various administrative/financial services for the Economic Development Authority (EDA). Economic Development (ED) did not have a Memorandum of Understanding (MOU) with the EDA that addressed which entity had job and oversight responsibilities for the various services provided to the EDA.

The City Attorney's Office indicated the following related to obtaining MOU's: "It is a long-standing legal principle that all agreements between parties should be reduced to writing to capture the rights, duties, obligations, terms and intentions of the parties. Without such, there is no legal obligation nor remedy for breach of the agreement."

We found that ED did not have an MOU that addressed the rights, duties, obligations, terms, and intentions of the parties. In addition, we found that job and oversight responsibilities for services provided to the EDA were not documented as to which entity had oversight responsibility for ED services provided.

This situation existed because the City did not have any documented procedures that articulated when MOUs should be required.

If this situation is not corrected, there is a potential risk that the City could be subject to financial loss and/or liability because they did not obtain a MOU.

Recommendation – The agreement between the ED and the EDA for providing various administrative/financial services should be reduced to writing using an MOU to capture the rights, duties, obligations, terms, and intentions of all the parties involved, and identify remedies for breach of the agreement.

Response: Though there have been no issues, concerns or disputes with the Economic Development Department employees performing various duties and functions as staff to the Economic Development Authority since at least 1998 (earliest start date of current staff members) and likely since the Economic Development Authority/Industrial Development

Authority inception in 1966, we do not dispute the finding for the need of an MOU between the EDA and Department of Economic Development/City of Chesapeake. We have engaged the City Attorney in creating an MOU for City Council and Economic Development Authority consideration, which will capture the rights, duties, obligations, terms, of the relationship between the City of Chesapeake, Economic Development Staff, and the EDA.

2. Development Agreements Updating

Finding – Development Agreement for Economic Development Investment Grant Program needs to be reviewed and amended to make clear that it is the grant recipient’s responsibility to notify ED/EDA when events occur that affect the terms of the Development Agreement.

It is a long-standing legal principle that all agreements between parties should be reduced to writing to capture the rights, duties, obligations, terms, and intensions of the parties. Without such, there is no legal obligation nor remedy for breach of the agreement.

In 2018, Project Cold Storage, applied to the Economic Development Authority (“EDA”) for a grant under the Economic Development Incentive Grant program. On December 11, 2018, City Council adopted a resolution authorizing a grant award, and appropriated \$300,000 to be transferred to the ED/ EDA for the grant. In December 2018, Project Cold Storage entered into a Development Agreement with the ED/EDA, which called for Project Cold Storage to construct a 107,000 sq. ft. facility expansion, invest at least \$12.5M in real estate, invest at least \$8,500,000 in equipment, and create at least 27 new jobs, all over 36 months.

Project Cold Storage was acquired by Company A, in March 2019 (the sale closed in May 2019). The State Corporation Commission website shows that Project Cold Storage was inactive, and its authorization to transact business in Virginia was automatically cancelled due to failure to pay the annual registration fee. The SCC shows that Company A as active, and qualified to transact business in Virginia.

The final Certificate of Occupancy (C.O.) for Project Cold Storage facility expansion was issued in November 2019. The ED/EDA was not aware at that time that Company A had acquired Project Cold Storage. When the ED/EDA became aware of the issuance of the final C.O., a check for \$100,000 representing payment of the first installment of the grant to Project Cold Storage was cut, but Company A returned the check, saying that they were not familiar with the existence of the grant and not interested in pursuing it. The EDA and ED staff were in the process of working with Finance to return the \$100,000 funds to the City.

The ED/EDA had not experienced this situation with prior grants. There was some lag time between the date of issuance of the final C.O., and the ED/EDA becoming aware that the C.O. had been issued. Project Cold Storage did not notify the ED/EDA that they were being acquired by Company A. In addition, our review of the Development Agreement revealed that the agreement did not articulate what information a company had to provide the ED/EDA (i. e. business being sold, permit number, Copy of C.O., Investment Grant

Program Worksheet completed before the second and third payments will be made).

This situation existed because this was the first time a company was sold before the project was completed in accordance with the Development Agreement. The agreement did not place the responsibility of providing required information on the company but rather made it the responsibility of the ED/EDA.

If this situation is not corrected the ED/EDA runs the risk of another company being sold prior to the completion of the Development Agreement without their knowledge. Also, not streamlining the receipt of the C.O. would continue to be an ineffective use of the ED/EDA staff's time and could result in delays issuing the first payment. In addition, by not requiring that the companies be responsible for properly returning the required paperwork puts on undue burden on the ED/EDA and may result in payment delays.

Recommendation – We recommend that consideration be given to review and amend the Development Agreement, to make clear that it is the grant recipients responsibility to notify the ED/EDA of any events and/or changes to their circumstances that may impact the recipient's performance under the Development Agreement. Also, the Economic Development Incentive Grant program policy may also need to be reviewed and amended to clarify the parties' reporting responsibilities.

We suggest the following items be considered:

- Obtain the permit number from the company at the beginning of the project than contact Development and Permits and provide them the permit number for the project and they will notify ED/EDA when the C. O. is issued.
- Require companies to provide ED/EDA a copy of the final C.O. when issued.
- Require companies to notify ED/EDA if the company is being sold.
- ED/EDA should indicate in the Development Agreement that companies be required to complete the Investment Grant program Worksheet before the second and third payments will be made. **(include number of days prior to due date of payment)**
- Contact Company A's management and offer them the same agreement as Project Cold Storage.
- The first \$100,000 payment written to Project Cold Storage should be returned to the City of Chesapeake. **(this was approved by the EDA Board on June 17, 2021, and the funds subsequently returned to the City)**

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters as they are responsible for crafting of Development Agreements. To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with

the City of Chesapeake Strategic Plan which will be in development soon.

3. Resolutions and Worksheet Calculations

Finding – Resolution amendments, approved by City Council, to the Economic Development Investment Grant Program, omitted tables that were referenced in the resolution.

The worksheet that ED/EDA used to determine the maximum amount of funds that were available for the Economic Development Investment Grant Program (EDIP) to a company, was not calculated in accordance with the Investment Grant Resolution dated July 12, 2016.

City resolutions should include all referenced tables and other information necessary for a complete and thorough understanding of the resolution. The affected department should review the resolution after it has been written to ensure that the resolution is correct, and complete, prior to council approval.

Commonwealth of Virginia Code § 15.2-1106. Control and management of affairs; books, records, accounts, etc., of agencies states: “A municipal corporation shall provide for the control and management of the affairs of the municipality, and may prescribe and require the adoption and keeping of such books, records, accounts and systems of accounting by the departments, boards, commissions, courts or other agencies of the local government as may be necessary to give full and true accounts of the affairs, resources and revenues of the municipal corporation and the handling, use and disposal thereof.”

Our review of the ED amendment adopted July 14, 2009 found that it did not include three of the eight referenced tables. Review of the ED amendment adopted July 12, 2016 found that it did not include the only table referenced in the amended resolution.

The EDIP Grant amounts were calculated using a point system. This point system assigned a point value for each of these seven attributes: jobs created, salaries, real estate investment, machinery and tools investment, business personal property investment, infrastructure improvements, and admissions tax. The total number of points were then multiplied by a preset value for example, \$5,000.00 per each 0.5 point. The actual grant amount would tend to be a fraction of this maximum. The maximum amount of the grant awarded could not exceed the expected tax revenues created from the amount the company invested in real estate, machinery, business personal property investments, and admissions tax for, in most projects, the first three years after completion of the project. Audit Services compared how the existing spreadsheet calculated the maximum amount of the grant with the calculation methodology contained in the Grant Resolution dated July 12, 2016. We found that three of the seven attributes, salary, machinery, and business personal property investments, were not calculated in accordance with the July 12, 2016 resolution amendment. Also, audit services found that the preset value, used to determine the maximum grant amount by being multiplied by the number of points, was not working as proposed in the amended resolution.

The resolutions were amending prior resolutions and only included those tables subject to being changed. The resolutions did, however, include references to additional tables that were not included and gave no indication of where the appropriate tables were to be found.

This situation was caused by an inadequate quality review by ED/EDA to ensure the resolution requested matched the resolution approved. The EDA was not aware that the amendment to the EDIP Grant Program resolution, dated July 12, 2016, had changed the method of calculating the points value of each attribute. The amendment moved to a formula-based approach from the original use of look up tables. In addition, the formulas allowed for half points between each whole point, which was not what the EDA had requested. These changes were not incorporated into the EDIP Grant Calculation Worksheet.

Not including all referenced tables in a resolution may create ambiguity as to what the resolution is trying to accomplish or what information is being addressed. The need for clarity is not achieved by the referencing of tables and either not including them or not indicating where they could be located. This may result in there being multiple tables being used from different sources. This could result in different people or departments interpreting the resolution in different ways with different results. Not including all referenced tables and other information may give rise to legal challenges and subsequently complicate the orderly function of government.

This caused the ED to not be in compliance with the current EDIP Grant Program resolution. Also, this lack of compliance introduced errors into the Economic Development Investment Grant Program Grant Calculation Worksheet. These errors understated the value of the maximum grant available. Since the ED based their grant offers as a percentage of this maximum there is the possibility that companies would receive a smaller grant offering because of these errors.

Recommendation – ED/EDA should ensure that all tables, and other material, referenced in resolutions, are in fact included, prior to them going before the City Council for approval. Develop a monitoring and oversight process for the review of resolutions. Change the Grant Calculation worksheet to reflect the calculation method that is included in the City Council amendment. Process a new amendment to correct the last amendment in order to have the calculations work as the EDA expected.

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the EDIP Resolution so that it is consistent with the Economic Development Department's Grant Calculation Worksheet. The Economic Development Department does not dispute this finding but will defer to the City Attorney and EDA Attorney on crafting of the EDIP Resolutions, with the input and careful review of Economic Development Staff. Economic Development acknowledges there was a minor inconsistency in the Grant Calculation Spreadsheet and has adjusted the calculations

accordingly. As a result of the minor inconsistency in the Grant Calculation Spreadsheet, no businesses received grant awards beyond what they were qualified. Neither the City of Chesapeake, nor any grant awardees, were negatively impacted by the Grant Calculation Spreadsheet inconsistency.

To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

4. Development Agreements – Signed Originals and Notary Issues

Finding – Official copies of development agreements (DAs) were found not to be signed, accurately notarized, properly dated or kept in a central location.

Best business practices require that:

- Contracts are properly dated.
- Contracts are signed by both parties.
- Signatures are properly notarized.
- Original copies are kept on file in a central location.

In “A HANDBOOK FOR VIRGINIA NOTARIES PUBLIC” it states: “A notary public is a public official whose powers and duties are defined by statute. A notary acts as an official, unbiased witness to the identity and signature of the person who comes before the notary for a specific purpose. The person may be taking an oath, giving oral or written testimony, or signing or acknowledging his or her signature on a legal document. In each case, the notary attests that certain formalities have been observed. The key function is to be certain that the person appearing before the notary is who that person claims to be. Notaries must constantly be aware that every notarial act affects the legal rights of others. Carelessness or negligence by the notary may injure these rights. A notary who fails to perform notarial acts lawfully and in good faith may be civilly liable for damages caused by their official misconduct. The employer of a notary may also be liable for the notary’s misconduct under certain conditions described later in this handbook.”

Audit Services selected 19 DAs for review. Between the ED/EDA files and those of the City Clerk’s office, copies of all the agreements were found. However, not all agreements were found in one area. Of those 19 DAs:

- 4 were not dated, or 21.05% (4/19).
- 17 of the DAs were signed by the EDA, or 89.47% (17/19).
 - 52.94% (9/17) had errors in the notarization.
 - 1, or 5.88% (1/17) was found not to be notarized at all.
 - Errors included leaving the date of the agreement off the notary stamp, using a wrong date for the agreement, and indicating that the agreement was signed before the date of the agreement.

- 15 of the DAs were signed by the Companies, or 78.95% (15/19).
 - 26.67% (4/15) had errors in the notarization.
 - 1 or 6.67% (1/15) was found not to be notarized at all.
 - Errors included leaving the date of the agreement off the notary stamp, using a wrong date for the agreement, and indicating that the agreement was signed before the date of the agreement.

In addition, one of the DAs had a pen and ink change made to the date of the DA without having the change properly initialed and dated by both parties.

The signed copies of the DAs were not being kept in a central location. Signed copies were not always being forwarded to the City Clerk's office. The notary issues were caused by not paying attention to detail and not requiring that all documents needing notarization be properly dated prior to being notarized.

Not having signed copies of contracts had the potential effect of not having a contract should it be challenged. The fact that documents were inaccurately notarized could potentially be a point of argument should there ever be a legal issue. To quote the handbook "Notaries must constantly be aware that every notarial act affects the legal rights of others. Carelessness or negligence by the notary may injure these rights. A notary who fails to perform notarial acts lawfully and in good faith may be civilly liable for damages caused by their official misconduct. The employer of a notary may also be liable for the notary's misconduct under certain conditions described later in this handbook."

Recommendation: Management should consider establishing quality assurance review procedures of DAs to ensure that completed, signed original development agreements are sent to the City Clerk's office as soon as executed.

The ED/EDA management should also consider:

- Ensuring that all development agreements are properly dated prior to being signed.
- Ensuring that all signatures are notarized.
- Sending the staff notary for refresher training on how to accurately notarize documents.
- Requiring that all notarizations be done correctly and reject inaccurate notarizations.
- Requiring that all pen and ink changes to the development agreements be initialed and dated by both parties.

Response: Economic Development does not dispute the findings. Since this Audit commenced a new staff member has been added to the Department with extensive legal experience and with significant experience as a Notary of Public with knowledge of procedures and guidelines set forth in Virginia Law. This staff member had been added to the Department review process to ensure all Development Agreements are complete, signed and properly notarized prior to being sent to the City Clerk. Economic Development is also investigating the use of digital signature software as an alternative solution to use of a Notary of Public.

5. EDIP Grant Payment Issue

Finding – The first EDIP Grant payments were not always processed in accordance with the development agreements (DAs).

Per the Code of Virginia Section 2.2-4352: “Every agency of local government that acquires goods or services, or conducts any other type of contractual business with a nongovernmental, privately owned enterprise, shall promptly pay for the completed delivered goods or services by the required payment date.”

We randomly selected ten EDIP grant DAs, to determine if the first payments were paid in accordance with the DAs. DA’s, selected for review, required that the first EDIP payment be made 60 days after the issuance of a certificate of occupancy. Our review of the DAs revealed that all had certificates of occupancy that were dated between June 9, 2017 and January 11, 2021. Of the ten agreements reviewed, 5 (50.0%) were paid as required, while 5 (50.0%) were paid after the agreed payment period had elapsed. The late payments averaged 168.4 days late and ranged between 129 and 230 days late.

**Table 4
Review of Development Agreements For 1st Payment**

Company	Per Agreement	Date of C/O	Date of 1st Payment	Timely Y/N	# of Days Past 60
Project Cold Storage	60 days	11/1/2019	6/18/2020	N	230
Winter Coats	60 days	12/13/2018	7/19/2019	N	218
Mother Goose	60 days	4/15/2019	8/1/2019	N	108
Jack Sprat	60 days	12/14/2020	5/20/2021	N	157
7 Standard Deviations	60 days	1/11/2021	5/20/2021	N	129
Ugly Duckling, Inc.	60 days	8/3/2018	8/15/2018	Y	0
Jay Poole and Associates	60 days	10/15/2020	10/20/2020	Y	0
Hampton Beverage Control	60 days	6/15/2017	8/7/2017	Y	0
Initial Consorts	60 days	6/9/2017	7/20/2017	Y	0
Electric Mixers	60 days	9/22/2020	11/10/2020	Y	0
					842
				Avg. # of Days Late	168.4
Total Checked	10				
Y	5	50.00%	Per Agreement		
N	5	50.00%	Not Per Agreement		

The COVID pandemic may have resulted in the 2 most recent payments being late as there was still disruption in the ED/EDA workflow. The remaining 3 were the result of certificates of occupancy being received late by the ED.

Not meeting the EDIP financial obligations, as stated in the DAs, puts the EDA out of compliance with their own agreements. This lack of compliance could raise doubt among potential business prospects about the EDA's veracity and make it harder to attract new businesses. Also, by not following the DAs the EDA risks reputational damage.

Recommendation – Management should ensure that all EDIP payments are paid in accordance with the DAs. In addition, management should develop and implement a monitoring process to ensure payments are made timely.

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters such as the crafting of Development Agreements.

6. Segregation of Duties

Finding – Economic Development (ED) maintains the financial records for the Economic Development Authority (EDA). We found that segregation of duties and compensating controls needed to be improved. In addition, there were no documented procedures in place for the disbursement process.

Best business practice indicates that no one person should be able to handle a transaction from beginning to end unless there are compensating internal controls in place. The AICPA states, "Segregation of Duties (SOD) is a basic building block of sustainable risk management and internal controls for a business. The principle of SOD is based on shared responsibilities of a key process that disperses the critical functions of that process to more than one person or department. Without this separation in key processes, fraud and error risks are far less manageable."

Our review of the financial records determined that an ED employee was responsible for maintaining the EDA financial records in Quick Books. We found that documented procedures had not been developed for the disbursement process.

Our review of the disbursement process revealed the following issues that need to be addressed. One individual performs the following functions which diminishes segregation of duties:

- Orders and receives prenumbered check stock for EDA.
- Controls unissued, issued, and void checks in a locked filing cabinet.
- Prepares and prints all checks for payments for the EDA for board member signatures. All issued checks require two board member signatures. **Note: Bank's do not verify authorized signatures on checks.** (except in special circumstances).
- Receives monthly bank statements with copies of issued checks (fronts only).
- Reconciles monthly bank statements.
- Prepares monthly reconciliements to present to the EDA board each month.
- Enters all deposits and disbursements into Quick Books.

- Assist outside accountants with annual audit.
- There was no back up for this position.

In addition, we found the following concerns related to compensating controls:

ED management received and reviewed the monthly bank statement with copies of all issued checks (fronts only) and reviewed the beginning and ending balance to the monthly bank reconciliation which was prepared by the person who maintained the Quick Books records. ED management presents reconciliements monthly at the EDA Board meeting.

- We found that all check numbers were not entered into Quick Books. Missing checks were not entered into Quick Books.
- Accountability for the numerical sequence for all issued, unissued, voided, and missing checks by an independent person was not in place.
- Fulton Bank unissued check stock needed to be destroyed. This checking account was closed in March 2019 and unissued checks was still being held in a locked filing cabinet.

This situation existed because procedures were not documented, and one person could handle the disbursement process from beginning to end. In addition, the compensating control process did not include the accountability of all issued, unissued, voided, and missing checks. Also, backs of checks were not received from the bank; therefore, endorsements were not being checked. If these situations are not addressed there is the risk that funds could be misappropriated. In addition, strong internal and compensating controls would better protect employees.

Recommendation: We recommend that documented procedures be established to ensure segregation of duties and compensating controls are in place. In addition, a monitoring process should be established to ensure internal controls are in place and functioning as designed.

The following items need to be addressed:

- All check numbers should be entered into Quick Books.
- If issued checks have forged signatures, the Bank does not verify that issued checks contain only authorized signatures.
- The numerical sequence of issued unissued, voided, and missing checks should be verified by an independent person on a periodic basis.
- Incorporate use of a missing checks report from Quick Books as part of the reconciliation review process.
- Consider requesting the bank to send EDA the front and backs of checks so that the endorsements can be reviewed.
- Fulton unissued check stock should be destroyed in the presence of two persons and the verification should document the beginning and ending numbers and the signatures and date of the two persons who verified the destruction of the checks.
- Develop a backup plan for this function in the case this person is out of the office for an extended period.

Response: The Economic Development Department does not dispute the findings and has address the following items as described above:

- *All check numbers should be entered into Quick Books.*
 - All checks are entered into Quick Books, including voided checks.
- *If issued checks have forged signatures, the Bank does not verify that issued checks contain only authorized signatures.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *The numerical sequence of issued unissued, voided, and missing checks should be verified by an independent person on a periodic basis.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *Incorporate use of a missing checks report from Quick Books as part of the reconciliation review process.*
 - Missing checks report is printed and reviewed by the Executive Secretary of the EDA on a monthly basis.
- *Consider requesting the bank to send EDA the front and backs of checks so that the endorsements can be reviewed.*
 - The front of checks are provided monthly as part of the bank statements and backs of checks are now being requested.
- *Fulton unissued check stock should be destroyed in the presence of two persons and the verification should document the beginning and ending numbers and the signatures and date of the two persons who verified the destruction of the checks.*
 - Closed Fulton Bank account check stock have been destroyed and verified by two people who signed and dated a statement confirming destruction.
- *Develop a backup plan for this function in the case this person is out of the office for an extended period.*
 - The EDA is contracting for Accounting and Audit Services and will include as part of these, back up accounting services in the event of an extended leave for Economic Development Staff member who performs monthly accounting functions for the EDA.

The Economic Development Department has procedures in place that include the Executive Secretary of the EDA to providing monthly review and oversight of the financial duties and functions performed by the Economic Development Staff on behalf of the EDA.

7. Petty Cash and Travel Funds

Finding – Documented procedures for petty/travel cash funds had not been developed, written, and implemented. Sufficient internal controls were not in place to safeguard these assets nor was Economic Development following Finance Department’s citywide Petty/Travel Cash procedures.

An effective petty/travel cash control process should incorporate the following attributes:

- Department should have documented petty/travel cash control procedures.
- Funds should be kept under the control of the person responsible for the funds.
- Funds should be counted at a minimum, on a quarterly basis.
- Counts should be documented on the Reconciliation Form.
- Counts should be performed by the person responsible for the fund and verified by a second person. Both individuals should sign the Reconciliation Form.
- If the designated petty/travel cashier changes, the petty/travel cash funds must be reconciled, and all receipts turned into Finance to replenish the petty/travel cash funds before the new petty/travel cashier takes over the funds. This audit process should include two employees at that site to ensure accuracy and to avoid fraud. Both employees should sign the Reconciliation Form.
- Funds should always be safeguarded.
- Receipts should be signed by the person receiving funds when issued and returned.
- Receipts for purchases should be reimbursed timely.
- Training provided for petty/travel cashiers.

We evaluated the internal control process for petty/travel cash funds and determined that internal controls were not in place and assets were not safeguarded. We found the following control weaknesses that need to be addressed:

- There were no documented department petty/travel cash fund procedures.
- Petty/travel cash funds was counted since July 17, 2019, and not counted again until July 2, 2020.
- The employee who was responsible for the petty/travel cash funds left the City's employ on July 2, 2020, and we were informed that the funds were counted by two individuals, but the physical count of funds was not documented on a Reconciliation Report and signed and dated by the individuals who counted and verified the funds.
- When the petty/travel cash funds custody change occurred on July 2, 2020, a memo had not been sent to notify Finance of the change in custody. Also, the petty cash receipt dated April 30, 2019, was not turned into Finance as required.
- Department was holding a petty cash receipt dated April 30, 2019, in the amount of \$23.40. This receipt was not processed until November 20, 2020. Also, receipt did not document the purpose of funds, date, and name/signature of the person who received the funds from petty cash.
- Petty/travel cash funds were maintained in a locked box and placed in a locked file cabinet. There was only one set of keys to both storage facilities which were always left in an unlocked desk drawer, which were accessible to five employees. **(This was corrected during our audit)**
- Petty/travel cash funds were issued to the management analyst, but the office coordinator was responsible for these funds. **(This was corrected during our audit)**

- We were informed that funds were to be conducted on a quarterly basis, but we found that counts were not counted quarterly.
- Our review of the records indicated that the petty cash (\$50), and travel fund (\$2000), were very seldom used. The travel fund was last used in 2018, and the petty cash fund was last used in April 2019. **The \$2000 travel fund was returned to Finance during our audit.**
- Reconciliation Report was not being signed and dated by the person that verified the funds.

These conditions existed because procedures were not documented, developed, and implemented for petty/travel cash funds and the safeguarding of assets. Also, no monitoring process had been developed and implemented to ensure controls were in place, and function as designed.

If petty/travel cash funds control procedures are not established and periodically monitored, the risk exist that cash funds could be misappropriated.

Recommendation – ED should develop and document petty/travel cash fund procedures so that cash funds are safeguarded. In addition, ED should develop a monitoring process to ensure adherence to petty/travel funds control procedures.

The following control procedures need to be addressed:

- Consideration should be given to eliminate petty/travel cash funds. **The \$2000 travel fund was eliminated during our audit.**
- Petty cash fund should be counted on a quarterly basis.
- Receipts should document name of person receiving funds, purpose and date funds were received.
- Finance should be notified in writing when custody of funds is changed.
- Receipts for issued funds should be replenished timely.
- Petty cash funds should be kept under the control of the person responsible for the fund.
- Petty cash should be counted on a quarterly basis by an independent person.
- Petty cash funds should be counted by custodian and verified by a second person and both individuals should sign and date the Reconciliation Report.

Response: Economic Development does not dispute the findings and as such has established and is following procedures requiring monthly counts with accompanying documentation (which exceeds City requirements of quarterly counts), and receipts for replenishment handled on a monthly basis. Additionally, Economic Development has eliminated the \$2,000 Travel Fund because it was used sparingly and not at all since the start of the Pandemic.

APPENDIX A: RESPONSE FROM ECONOMIC DEVELOPMENT OFFICIALS



Memorandum

TO: Darren M. Padilla, Acting City Auditor
Edwin "Keith" Jeter, Audit Services

FROM: Steven C. Wright, Director of Economic Development

RE: Internal Audit Report – Economic Development

A handwritten signature in black ink, appearing to read "SC Wright", with a flourish underneath.

The Economic Development department has reviewed the findings of the internal audit conducted by Audit Services staff. We have provided responses to the recommendations contained with the audit.

As indicated in our responses, the Economic Development department does not dispute the findings but will defer to the City Attorney on legal matters as they are responsible for crafting of a Memorandum of Understanding, Development Agreements and Resolutions for the EDIP. To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

Economic Development appreciates the Audit Department's approach to performing this audit, as they were professional and courteous in interacting and performing their work. We will use the findings as an opportunity to continue our process improvement and be as efficient as possible in fulfilling our mission of assisting prospective and existing businesses to grow the City's tax base and create jobs for our citizens.

If you have any questions, please call me at 382-8040.

676 Independence Parkway, Suite 200
Chesapeake, VA 23320
(757) 382-8040 / chesapeakeva.biz



Economic Development – Responses

1. Memorandum of Understanding

Response: Though there have been no issues, concerns or disputes with the Economic Development Department employees performing various duties and functions as staff to the Economic Development Authority since at least 1998 (earliest start date of current staff members) and likely since the Economic Development Authority/Industrial Development Authority inception in 1966, we do not dispute the finding for the need of an MOU between the EDA and Department of Economic Development/City of Chesapeake. We have engaged the City Attorney in creating an MOU for City Council and Economic Development Authority consideration, which will capture the rights, duties, obligations, terms, of the relationship between the City of Chesapeake, Economic Development Staff, and the EDA.

2. Development Agreements Updating

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters as they are responsible for crafting of Development Agreements. To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

3. Resolutions and Worksheet Calculations

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the EDIP Resolution so that it is consistent with the Economic Development Department's Grant Calculation Worksheet. The Economic Development Department does not dispute this finding but will defer to the City Attorney and EDA Attorney on crafting of the EDIP Resolutions, with the input and careful review of Economic Development Staff. Economic Development acknowledges there was a minor inconsistency in the Grant Calculation Spreadsheet and has adjusted the calculations accordingly. As a result of the minor inconsistency in the Grant Calculation Spreadsheet, no businesses received grant awards beyond what they were qualified. Neither the City of Chesapeake, nor any grant awardees, were negatively impacted by the Grant Calculation Spreadsheet inconsistency.

To seek continual improvement, the Economic Development and City Attorney are reviewing the entire Economic Development Investment Program (EDIP) for items that need immediate attention and hope to engage the City Manager, City Council and EDA in an overhaul of the EDIP so that it better meets the needs of the City and Businesses and is aligned with the City of Chesapeake Strategic Plan which will be in development soon.

4. Development Agreements – Signed Originals and Notary Issues

Response: Economic Development does not dispute the findings. Since this Audit commenced a new staff member has been added to the Department with extensive legal experience and with significant experience as a Notary of Public with knowledge of procedures and guidelines set forth in Virginia Law. This staff member had been added to the Department review process to ensure all Development Agreements are complete, signed and properly notarized prior to being sent to the City Clerk. Economic Development is also investigating the use of digital signature software as an alternative solution to use of a Notary of Public.

5. EDIP Grant Payment Issue

Response: The Department has engaged the City Attorney in reviewing and amending (as they deem necessary) the Development Agreement format. The Economic Development Department does not dispute this finding but will defer to the City Attorney on legal matters such as the crafting of Development Agreements.

6. Segregation of Duties

Response: The Economic Development Department does not dispute the findings and has address the following items as described above:

- *All check numbers should be entered into Quick Books.*
 - All checks are entered into Quick Books, including voided checks.
- *If issued checks have forged signatures, the Bank does not verify that issued checks contain only authorized signatures.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *The numerical sequence of issued unissued, voided, and missing checks should be verified by an independent person on a periodic basis.*
 - The Executive Secretary of the EDA reviews bank statements, reconciliations, all checks (issued, outstanding, and voided) on a monthly basis and reports findings to EDA monthly.
- *Incorporate use of a missing checks report from Quick Books as part of the reconciliation review process.*
 - Missing checks report is printed and reviewed by the Executive Secretary of the EDA on a monthly basis.
- *Consider requesting the bank to send EDA the front and backs of checks so that the endorsements can be reviewed.*

- The front of checks are provided monthly as part of the bank statements and backs of checks are now being requested.
- *Fulton unissued check stock should be destroyed in the presence of two persons and the verification should document the beginning and ending numbers and the signatures and date of the two persons who verified the destruction of the checks.*
 - Closed Fulton Bank account check stock have been destroyed and verified by two people who signed and dated a statement confirming destruction.
- *Develop a backup plan for this function in the case this person is out of the office for an extended period.*
 - The EDA is contracting for Accounting and Audit Services and will include as part of these, back up accounting services in the event of an extended leave for Economic Development Staff member who performs monthly accounting functions for the EDA.

The Economic Development Department has procedures in place that include the Executive Secretary of the EDA to providing monthly review and oversight of the financial duties and functions performed by the Economic Development Staff on behalf of the EDA.

7. Petty Cash and Travel Funds

Response: Economic Development does not dispute the findings and as such has established and is following procedures requiring monthly counts with accompanying documentation (which exceeds City requirements of quarterly counts), and receipts for replenishment handled on a monthly basis. Additionally, Economic Development has eliminated the \$2,000 Travel Fund because it was used sparingly and not at all since the start of the Pandemic.