October 18, 2021

Lisa M. Murphy, Chair
City of Virginia Beach Development Authority
4525 Main Street, Suite 700
Virginia Beach, VA 23462

Subject: Follow-Up Review of the City Auditor’s 2018 Audit of the City of Virginia Beach Development Authority

Dear Ms. Murphy,

We have performed a follow-up review of our 2018 Audit of the City of Virginia Beach Development Authority’s (VBDA) Economic Development Investment Program (EDIP) to determine whether our audit recommendations were implemented.

We were not engaged to perform and did not perform an audit, the objective of which would have been the expression of an opinion or limited assurance. Accordingly, we do not express such an opinion. Had we performed additional procedures; other matters may have come to our attention that would have been reported to you. We completed the procedures on August 13, 2021.

This report is intended solely for the information and use of the VBDA, the City Manager’s Office, and City leadership. It is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

This engagement was conducted in accordance with Government Auditing Standards (GAS). GAS incorporates financial and attestation standards established by the American Institute of Certified Public Accountants. These standards also provide guidance for performing and reporting the results of agreed-upon procedures. The sufficiency of these procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described herein, either for the purpose for which this report has been requested or for any other purpose.
The Office of the City Auditor reports to City Council through the Audit Committee and is organizationally independent of all City departments. This report will be distributed to the City’s Audit Committee, City Council, City Manager, the VBDA, and appropriate management within the City. This report will also be made available to the public through the Office of the City Auditor’s webpage.

**Background**

The City’s economic development efforts to expand the tax base through increased business investment are governed by the VBDA, which was established in 1964 as a component, but legally separate unit of the City. The VBDA is supported by the City’s Economic Development Department (Economic Development).

The VBDA, through Economic Development, focuses on attracting and retaining domestic and international business that will bring new capital investment and jobs to Virginia Beach. It provides a variety of services to help businesses: customized market research, building or site search, permitting and development assistance, and other useful resources.

The EDIP is one of the resources that the VBDA administers. It provides discretionary grants to qualifying businesses that are relocating to or expanding in Virginia Beach in support of economic development projects that create new jobs and capital investments. The average yearly funding for the last three fiscal years was $2.3 million, which comes from the allocation of 16 cents of cigarette tax collected for every pack sold.

The EDIP grants are based on the average annual salary and number of new jobs created, and/or new capital investments made over a performance period of 36 months or 48 months for Naval Air Station Oceana’s Accident Potential Zone – One (APZ-1) awards. Policies and procedures over this program are set forth in the EDIP Policy.

- **Part A** covers qualifying new businesses who relocate to Virginia Beach and existing businesses who remain or expand operations within Virginia Beach.

- **Part B** covers qualifying developers and property owners for development or redevelopment of properties in Strategic Growth Areas, Special Economic Growth Areas, Economic Redevelopment Areas, or Opportunity Zones.

- **Part C** covers qualifying developers and property owners for the development or redevelopment of properties in APZ-1 or Clear Zones.

- **Part D** covers general provisions applicable to Parts A, B, and C.
Based on our review, we found the following issues:

**Parts A – C: Capital Investment Criterion**

**Finding 1. Inadequate Supporting Documentation for Machinery and Tools**
One recipient received EDIP funds for capital investment in new machinery and tools, but the supporting documentation provided was solely generated by the recipient, i.e., an unfiled Tangible Personal Property/Machinery & Tools Return (CR-13) accompanied by a list of business personal property. Proper support for the disbursement of EDIP funds should be third-party documentation, such as vendor invoices and/or the business tangible property tax bill, which serves as evidence that the CR-13 was successfully filed with the Commissioner of the Revenue’s Office.

Recommendation:

1.0 Evaluate the appropriateness of documents provided by the recipient.

**Parts A – C: New Jobs Criterion**

**Finding 2. No Effective Process in Place to Verify Recipient’s Performance**
The VBDA awarded an EDIP grant of $350,000 with the understanding that Virginia Beach would receive 147 full-time equivalent (FTE) positions. However, this grant was awarded without an
effective process in place to measure and ensure how the FTE positions are going to be filled. The absence of an effective process to verify performance at the time of the award increases the risk of inaccurate disbursements.

**Recommendations:**

2.0 Ensure that an effective process of verifying performance is developed at the time of the EDIP grant award.

**Finding 3. Filling of Job Positions not According to the EDIP Policy**

Of the disbursements made by Economic Development to nine recipients for job expansion and retention, we found that the positions were not filled according to the EDIP policy, in that:

- Seven recipients received funds for positions that were filled less than one year. This is inconsistent with the EDIP Policy requirement that states, “For any job to qualify for an award, that position must be filled for at least one year.” An email in one of the recipients’ folder mentioned that disbursement could be made at the Department Director’s discretion. However, the EDIP Policy makes no mention of this discretion nor does it have anything other than the one sentence requirement.

- Two recipients had positions filled before their resolution was adopted by the VBDA. The resolution date is the official start of the grant and only those positions created from that date and up to 36 months thereafter are considered part of the performance period.

**Recommendations:**

3.0 Revise the EDIP Policy to include more detail on the job expansion and retention criteria.

3.1 Ensure that disbursements are made only: 1) for positions filled or retained within the performance period and 2) after the positions were filled for more than one year.

**Finding 4. Inadequate Supporting Documentation for Job Expansion**

Due to the large amounts of EDIP funds disbursed, we deem that proof of performance for job expansion and retention should be supplemented by a stronger form of evidence, such as a computerized Human Resources employee report. Currently, the recipient merely needs to submit a memo attesting to the accuracy and completeness of the accompanying list of employees. The current list is a Microsoft Excel spreadsheet that contains the job position, date position filled, location, and annual salary of every employee. We deem this type of support as inadequate, as errors could have easily been made or entries falsified. For instance, when we performed a reasonableness review, we observed some unusual entries:
- A recently hired processor is paid a salary that is 1.5 times higher than the average salary for processors in the business. This processor (staff level position) was the fourth highest-paid among 84 employees, higher than the salaries of most managers and an attorney.
- A recently hired manager’s salary is twice more than another manager’s salary who has been employed by the recipient for more than a decade and is also its longest standing employee.

We have not performed any further verification on the observations above, so we are not suggesting that the information provided was incorrect or that impropriety has occurred. We just want to highlight the benefit of having a supplemental, stronger form of evidence to gain more assurance.

Recommendations:

4.0 Require a strong, supplemental form of evidence to ensure that disbursements for job expansion/retention is properly made to strengthen the integrity of the EDIP process.

4.1 Determine the State’s method for verifying job creation and, where possible, align with the State’s methodology.

4.2 Due to heavy involvement in the disbursements process, have the VBDA Accountant sign the disbursement routing sheet to show that he or she has reviewed the accompanying documentation. The signature will be in addition to those of the Business Development Manager, the Department Director, and the Senior Attorney from the City Attorney’s Office.

Part D General Provisions

Finding 5. Exact Amount of Incentive Funds Available is Currently Unknown to the VBDA

Currently, the exact amount of Incentive funds available is unknown to the VBDA. Due to the VBDA Accountant’s departure, the last report of the Incentive Accounts’ Payables and Commitments balance was in January 2021, which presented December 2020’s month-end balance of $1.7 million. This was an aggregation of all economic incentive programs’ individual balances that included EDIP Parts A – D. While subsequent monthly cash flow presentations to VBDA included disbursements, they did not show the Incentive Funds balance. Not knowing the exact amount of available funds creates a risk that VBDA could overcommit funds.

Recommendation:

5.0 Refrain from further awarding any EDIP grants until the exact amount of available funds is determined and made available to the VBDA.
Finding 6. EDIP Total Incentive Awards Spreadsheet Needs to be Updated

The Total Incentive Awards spreadsheet, which is the primary record for tracking and summarizing all important information about EDIP awards, has not been updated since the VBDA Accountant’s departure in February 2021. It is critical that this spreadsheet is continually maintained by Economic Development so that management and the VBDA are aware of the status of EDIP grants and can identify available funds from projects that have ended.

Based on our analysis of the spreadsheet, we noted that:

- There is $596,000 of potentially available EDIP funds that could be recommitted to funding future projects. This is the total undisbursed awards from projects that have ended but not closed, the earliest of which were from fiscal year 2014. Tables 1 and 2 below show this and other results of our analysis.

- It does not adequately depict where the award truly stands. For example, the user of the spreadsheet would not know why there was zero disbursement for a project that has ended.

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<th>#</th>
<th>Total Award</th>
<th>Total Disbursed</th>
<th>Potential Funds Available</th>
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<tr>
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<td>Performance period ended but not closed &amp; not paid 100%</td>
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</tr>
<tr>
<td>2</td>
<td>Performance period ended but not closed &amp; zero paid</td>
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<td>$30,000</td>
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<tr>
<td>3</td>
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<td>Payment made but not performed*</td>
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<td>Award for jobs expansion but no entry in jobs columns</td>
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*The City is filing a claim in bankruptcy court.

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<th>#</th>
<th>Total Award</th>
<th>Total Disbursed</th>
<th>Potential Funds Available</th>
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Recommendation:

6.0 Analyze and update the Total Incentive Awards spreadsheet to ensure that it properly reflects the status of the projects and to determine the amount of available funds that can be used for future projects.
Finding 7. Program Training Needed
Based on our confidential staff survey and interviews, as well as the results of our documentation review, we found that the level of knowledge of business development managers on the EDIP policy and process is not consistent in some areas, particularly in their answers to the following questions:

- When is a recipient eligible for disbursement?
- Who performs verification of documents received from the recipient?
- Who ensures that all requirements have been met at the conclusion of the grant?
- When can EDIP funds be disbursed for a filled position?
- What takes place when the disbursement proposal is presented to management?

Seventy-five percent of the Business Development Managers are less than two years in their position and are trained by their seniors. However, the training is informal and can be inconsistent, as they are based on the level of expertise and experience of the trainers.

Furthermore, there is a general understanding among Business Development Managers that the EDIP grant process is a minor portion of their responsibilities, and that the VBDA Accountant is almost solely responsible for all financial-related matters. However, we deem that increasing their knowledge and involvement in financial matters is critical to better management of their projects.

Recommendation:

7.0 Given the considerable size of the EDIP funds awarded management should take this time to develop a formal training program for Business Development Managers.

Our findings and recommendations have been discussed and agreed upon with management.

We would like to thank the management and staff from the Department of Economic Development for their courteous assistance during our engagement.

Should you have any questions, please do not hesitate to contact me at 385-5872 or via e-mail at lremias@vbgov.com.

Sincerely,

Lyndon S. Remias, CPA, CIA
City Auditor
LSR/ag

c: Patrick A. Duhaney, City Manager
   Taylor V. Adams, Director, Economic Development
   Alex W. Stiles, Senior Attorney, City Attorney’s Office
   City of Virginia Beach Development Authority
   Letitia L. Shelton, Director, Finance
October 15, 2021

Office of the City Auditor  
Attention: Lyndon S. Remias, CPA, CIA  
City of Virginia Beach  
Municipal Center, Bldg. 1, Rm. 334  
Virginia Beach, VA 23456

Subject: Follow-Up Review of the City Auditor’s 2018 Audit of the City of Virginia Beach Development Authority

Dear Mr. Remias:

This letter is in response to your office’s follow-up review of the 2018 Audit of the City of Virginia Beach Development Authority’s (VBDA) Economic Development Investment Program (EDIP). In the October 7, 2021 letter, you advised that your office was determining whether your audit recommendations were implemented since 2018 and was not engaged to perform and did not perform an audit. Your staff spent approximately six weeks at the Economic Development Department reviewing files, interviewing staff and completed its work on August 13, 2021. After that research was completed, we met together several times over the past month with Economic Development leadership to arrive at the findings and recommendations described in your correspondence, which will lead to process improvements benefitting all of our programs. We accept the findings and intend to implement the recommendations.

We would like to thank you and your staff for your work and professionalism throughout the process. If you have any questions, please do not hesitate to contact me or Taylor Adams.

Sincerely,

Lisa M. Murphy  
Chair

Attachment: Follow-Up Review of the City Auditor’s 2018 Audit of the City of Virginia Beach Development Authority – letter dated October 7, 2021

cc: Virginia Beach Development Authority members  
Patrick A. Duhaney, City Manager  
Taylor V. Adams, Deputy City Manager/Economic Development Director  
Alexander Stiles, Senior Attorney, City Attorney’s Office  
Letitia L. Shelton, Director of Finance