

Internal Audit Department
NeighborWorks® America

**Audit Review of
External Business Relationships –
Neighborhood Risk Management
Corporation (NRMC)**

Project Number: NWA.EBR.2013

**Audit Review of the External Business Relationship with
Neighborhood Risk Management Corporation**

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June 19, 2013

To: NeighborWorks America Audit Committee

Subject: Audit Review of the External Business Relationship with Neighborhood Risk Management Corporation

Please find enclosed the final audit report of the External Business Relationship with Neighborhood Risk Management Corporation. Please contact me with any questions you might have.

Thank you.

Frederick Udochi
Director of Internal Audit

Attachment

cc: E. Fitzgerald
M. Forster
C. Wehrwein
J. Bryson
B. Finn
T. Deyo

Function Responsibility and Internal Control Assessment
Audit Review of the External Business Relationship with Neighborhood Risk
Management Corporation

Business Function Responsibility	Report Date	Period Covered
National Initiatives and Applied Research (NIAR)	June 19, 2013	NRMC and NeighborWorks Business relationship/structure as of May 2013
Assessment of Internal Control Structure		
Effectiveness and Efficiency of Operations	Generally Effective¹	
Reliability of Financial Reporting	Not Applicable	
Compliance with Applicable Laws and Regulations	Not Applicable	

This report was conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing*.

¹ **Legend for Assessment of Internal Control Structure:** **1. Generally Effective:** The level and quality of the process is satisfactory. Some areas still need improvement. **2. Inadequate:** Level and quality of the process is insufficient for the processes or functions examined, and require improvement in several areas. **3. Significant Weakness:** Level and quality of internal controls for the processes and functions reviewed are very low. Significant internal control improvements need to be made.

Executive Summary of Observations, Recommendations, and Management Responses

Summarized Observation; Risk Rating	Management Agreement with Observation (Yes/ No)	Internal Audit Recommendation Summary	Accept IA Recommendation (Yes/ No)	Management's Response to IA Recommendation	Estimated Date of Implementation (Month/Year)	Internal Audit Comments on Management Response
<p>Observation No. 1 Independent Objective Review(s) of NRMC</p> <p>An independent objective Program Review by OAD has not been conducted over the programmatic/operational capacity of NRMC since inception. In addition, an OAD financial analysis has not been conducted since inception.</p> <p>Risk: (b) (4)</p>	Yes	<p>Recommendation No. 1 OAD Independent Objective Program Review and Financial Analysis</p> <p>We recommend an OAD Program Review be conducted within the next 12 months (September 2014) to evaluate the programmatic and operational capacity of NRMC to carry out its mission.</p> <p>We also recommend OAD conduct a financial analysis of NRMC's most recently issued financial statements prior to the issuance of future grant awards.</p>	Yes	<p>Management agrees that a Program Review be conducted by OAD within the next 12 months (Sept'14). This review will evaluate NRMC's operational and programmatic capacities that impact its ability to successfully deliver on its mission.</p> <p>Management also agrees OAD should conduct a financial analysis on the most recent financial statements for NRMC. This will be complete prior to the issuance of further grant awards.</p>	<p>OAD Program Review completed by September 2014</p> <p>Audit review to be conducted on next NRMC fiscal year audit; anticipated by end of September 2013</p>	Internal Audit accepts Management's response.

Summarized Observation; Risk Rating	Management Agreement with Observation (Yes/ No)	Internal Audit Recommendation Summary	Accept IA Recommendation (Yes/ No)	Management's Response to IA Recommendation	Estimated Date of Implementation (Month/Year)	Internal Audit Comments on Management Response
<p>Observation No. 2 Retroactive Adjustments to Cash Collateral Account</p> <p>Per review of the grant funding request from NRMCM, Internal Audit noted that NRMCM elected to "closeout" its 2006 GL policy with the (b) (4) resulting in (b) (4) processing retroactive adjustments to the cash collateral account totaling approximately \$400,000. At the time the adjustments were made, (b) (4) unable to explain the retroactive adjustments and to NRMCM's knowledge the adjustments were contrary to its understanding of the structure and economics of the program. As a result, the adjustment was accounted for in NRMCM's 2011 financial statements. As at the close of this review NRMCM asserted that it is following up on the matter to determine the proper recourse and if any funds may be recovered.</p> <p>Risk Rating (b)</p>	<p>Yes</p>	<p>Recommendation No. 2 Follow Up on (b) (4) Retroactive Adjustments</p> <p>As a result of our review of the funding request, Internal Audit recommends NeighborWorks follow up on the progress of the (b) (4) dispute in order to understand the status and any subsequent resolution. Internal Audit notes a program review may be the appropriate medium to facilitate the follow up. See report observation no. 1 above.</p>	<p>Yes</p>	<p>Management agrees that NeighborWorks America should remain informed on the progress of the (b) (4) dispute. Management agrees to remain in contact with NRMCM regarding the dispute and will stay informed on all updates on status and any subsequent resolution.</p>	<p>The dispute is a matter between NRMCM (b) (4) NeighborWorks America has no control over any resolution between these two third parties. However, NRMCM informs us that discussions are ongoing and are hopeful a resolution will soon be reached. In any event, NeighborWorks America will stay informed and suggest OAD follow-up on this in their program review.</p>	<p>Internal Audit accepts Management's response and agrees that this is a matter between NRMCM (b) (4) Internal Audit is of the opinion that the nature and extent of identified risk events (external and internal) should be evaluated by the Corporation in the event of future grant awards for continued business relationship.</p>

Risk Rating Legend:

Risk Rating: HIGH

A serious weakness which significantly impacts the Corporation from achieving its corporate objectives, financial results, statutory obligations or that may otherwise impair the Corporation's reputation.

Risk Rating: Moderate

A control weakness which could potentially undermine the effectiveness of the existing system of internal controls and/or operational efficiency, integrity of reporting and should therefore be addressed.

Risk Rating: Low

A weakness identified which does not seriously detract from the system of internal control and or operational effectiveness/efficiency, integrity of reporting but which should nonetheless be addressed by management.

Management Response to the Audit Review of the External Business Relationship (EBR) with the Neighborhood Risk Management Corporation (NRMC)		
# Of Responses	Response	Recommendation #
2	Agreement with the recommendation(s)	1, 2
0	Disagreement with the recommendation(s)	N/A

Background

Neighborhood Risk Management Corporation (NRMC) is an independent 501(c) (3) nonprofit organization organized in 2005 by NeighborWorks America. NRMC is a collaborative member-driven organization established as a mechanism by which NeighborWorks network organizations may obtain insurance and alternative risk coverage which in many cases is not available to its members in the traditional insurance market. NRMC products cover a range of risk reduction programs and broader insurance coverage at rates lower than those in the traditional markets.

NRMC utilizes the insurance broker Willis to aid in the acquisition and negotiation of insurance products for its members in all 50 states of which Willis is licensed. The NRMC group insurance program is available to members with multifamily and commercial properties within its portfolio. The following insurance products are available - property, general liability, casualty, auto liability and physical damage, and umbrella liability. As of January 2013, NRMC's portfolio was comprised of 66 member organizations, with 33,921 units valued at approx. \$3.97 billion.

In addition to providing members with access to insurance products, NRMC provides educational training programs in the areas of risk reduction, loss mitigation, and other related topics in order to meet the risk management educational needs of its members.

Since inception NRMC has been run by the collective efforts of its board of directors and a NeighborWorks NIAR staff serving as a key liaison. The liaison was responsible for providing administrative/professional services which included the coordination/staffing of board meetings and policy/product development. However, in March 2012, NRMC hired its first Executive Director Deborah S., Aschheim. As such the role and involvement of NeighborWorks in NRMC has been de-emphasised significantly from the daily operations of the organization to more of an administrative advisory role.

NeighborWorks has provided NRMC with several restricted (capital) and non restricted (expendable) grant awards since inception. Restricted grant awards total \$1.2 million since 2005, with the most recent award of \$200K in September 2012 to aid NRMC in meeting its retention shortfall. Non restricted grant awards to date from NeighborWorks America total \$338K, with the most recent award totaling \$130K in September 2012 (\$100K) and March 2013 (\$30K) to support the further development of its efforts of risk management through education and services and consulting services.

Objective

The objective of the audit was to:

- Review and evaluate the contractual relationship between NeighborWorks America and Neighborhood Risk Management Corporation;
- Obtain assurance that oversight activities put in place are sufficient and relevant;
- Ensure the issuance of grant awards were consistent with the grant award process to non-network organizations.

Scope

The scope of the review included an examination of the Neighborhood Risk Management Corporation business relationship with NeighborWorks America (the external business relationship) as of May 2013² (See Appendix) and the oversight risk management activities put in place by NWA management. The scope also included grant awards made in FY 2012 and 2013. Internal audit did not conduct any audit review onsite at the NRMC office premises and our review was limited to relevant documentation provided by NeighborWorks management and inquiries of relevant NIAR staff in respect of NRMC.

Methodology

Internal Audit requested and received the following:

- 2010 Administrative Services Agreement between NeighborWorks America and NRMC and the current Amendment to Exhibit A (executed in FY 2013)
- September 25, 2012 Grant Agreement
- March 12, 2013 Grant Agreement

Internal Audit distributed a questionnaire to increase our understanding of the NRMC relationship and reviewed documentation supporting the grant awards issued in September 2012 and March 2013.

In addition Internal Audit reviewed NRMC certificate of incorporation, bylaws, corporate policies and procedures, Form 990 and financial statements.

² This relationship is articulated in the most recent Administrative Services Agreement between NRMC and NWA.

Observations and Recommendations

Observation No. 1 – Independent Objective Review of NRMC

In any external business relationship there can be potentially significant financial, legal and compliance risks associated with such relationships. It is important that as part of NWA's risk management oversight activities plans are in place to identify internal risks and control gaps related to processes that directly affect third party external business relationships such as NRMC. One such critical activity the Corporation has deployed in the past on similar relationships is the program review.

Program Reviews evaluate the programmatic and organizational capacity of an organization to fulfill its mission and purpose. The Organization Assessment Division (OAD) conducts program reviews of organizations for which NeighborWorks has an external business relationship. Based on our review we noted that an independent objective review has not been conducted over the programmatic/operational capacity of NRMC since inception.

In addition to a program review, OAD conducts a financial analysis over the audited financial statements of potential grantees. We note that an OAD financial analysis has not been conducted over the financial statements prior to the issuance of grant awards.

Recommendation No. 1 – OAD Independent Objective Program Review and Financial Analysis

We recommend an OAD Program Review be conducted within the next 12 months (September 2014) to evaluate the programmatic and operational capacity of NRMC to carry out its mission.

Internal Audit notes the completion of a Program Review will provide management with insight as to whether or not NRMC has the capacity to fulfill its mission and also identify any internal risks or control gaps as part of the monitoring of this business relationship.

We also recommend OAD conduct a financial analysis of NRMC's most recently issued financial statements prior to the issuance of future grant awards. A financial analysis will provide NeighborWorks insight into the financial stability of NRMC.

Internal Audit notes that conducting the Program Review and the Financial Analysis will aid NeighborWorks in competently managing its risk appetite/exposure in relation to NRMC.

Observation No. 2 –Retroactive Adjustments to Cash Collateral Account

During our review of the September 2012 grant award made to NRMC, Internal Audit reviewed the grant funding request from NRMC, noting that NRMC elected to "closeout" its 2006 GL policy with the (b) (4) resulting in (b) (4) processing retroactive adjustments to the cash collateral account totaling approximately \$400,000. At the time the adjustments were made, (b) (4) was unable to explain the retroactive adjustments and to NRMC's knowledge the adjustments were contrary to its understanding of the

structure and economics of the program. As a result, the adjustment was accounted for in NRMC's 2011 financial statements. At the close of this review, NRMC asserted that it is following up on the matter to determine its recourse and if any funds may be recovered.

Recommendation No. 2 – Follow Up on (b) (4) Retroactive Adjustments

As a result of our review of the funding request, Internal Audit recommends that NeighborWorks follow up on the progress of the (b) (4) dispute as part of any planned future Program Review to understand the status and any subsequent resolution. See report observation no. 1 above.

Conclusion

In the absence of effective risk management oversight activities NWA could be exposed to increased business risk and having a consistent and effective monitoring plan in place would help to further mitigate such risks. The addition of a Program Review which is primarily done onsite would only serve to enhance the current activities in place.

APPENDIX A – NRMCA Administrative Services Agreement (including Appendix A)

ADMINISTRATIVE SERVICES AGREEMENT

This ADMINISTRATIVE SERVICES AGREEMENT ("Agreement") is made and entered into as of the 19th day of April, 2010, by and between Neighborhood Reinvestment Corporation ("NR") and Neighborhood Risk Management Corporation ("NRMCA"), a Delaware not-for-profit corporation.

WITNESSETH

:

WHEREAS, NR wishes to assist NRMCA through the provision of various operational and administrative services; and

WHEREAS, NRMCA desires to retain NR for the purpose of providing such services as described herein;

NOW THEREFORE, it is agreed by and between the parties hereto as follows:

1. Retention of NR. NRMCA hereby retains NR to provide the services described on Exhibit A attached hereto and by this reference made a part hereof, as such Exhibit A may be amended from time to time.
2. Compensation. In consideration of the services, NRMCA agrees to compensate NR in accordance with the compensation methodology described on Exhibit A attached hereto and by this reference made a part hereof, as such Exhibit A may be amended from time to time.
3. Annual Services and Compensation Review. The parties acknowledge that, during the course of this Agreement, they may mutually decide to amend Exhibit A, as necessary and appropriate to advance and promote the purposes of this Agreement. Each party shall provide to the other party, not later than February 1 of each year, the text of any proposed amendments to Exhibit A, if any. Upon receipt of proposed amendments, the parties shall exercise their best efforts to agree on a mutually satisfactory amendment by March 31 of each year. If the parties are unable to agree on the form of amendment by such date, then such dispute shall be resolved in accordance with the dispute resolution provisions of Section 10 below. After agreement is reached as to the form of amendment, such amendment shall be submitted by NRMCA within ten (10) days to any necessary Federal or state agency for such agency's approval, with the intent that such amendment shall become effective as of the later of April 1 of the next year or the date upon which regulatory approval is obtained.

4. Limited Authority. Nothing herein shall diminish, or be deemed to diminish, the independent legal existence and authority of NRMC, its board of directors, members, or employees.

5. Term and Termination. The term of this Agreement shall commence on the date first above written and shall continue for a two (2) year period unless sooner terminated as permitted herein. This Agreement thereafter shall be renewed for four (4) subsequent periods of two (2) years each without additional action unless either party provides notice to the other party not later than one hundred twenty (120) days prior to the expiration of the then-existing term that such party desires not to renew this Agreement. This Agreement may be terminated at any time upon the mutual agreement of NR and NRMC. This Agreement may also be terminated for cause (as defined in Section 10 below) after application of the dispute resolution procedure set forth in Section 10 below. Upon the occurrence of any termination, NR and NRMC shall be liable to each other for all services required to be performed, and all compensation required to be paid, through the effective date of termination.

6. Confidentiality. NR agrees that all business records and information of any type or description which are created, used, disclosed to, or otherwise learned by it as a result of this Agreement shall be deemed to be confidential and proprietary information, and NR agrees that it shall not reveal, publish, communicate or otherwise disclose such information to a third party without the other party's prior written consent. Notwithstanding the foregoing, NR may reveal or use any information that is publicly available or is necessary for purposes of analysis and evaluation by others in the performance of NR's obligations hereunder. Upon termination of this Agreement, NR will return to NRMC any books, records, reports, or any other documents or other property relating to NRMC or its business. The provisions of this paragraph relating to the treatment of confidential and proprietary information shall remain in full force and effect indefinitely, or until such date as the parties may mutually agree. NRMC shall, during the term of this Agreement, be given reasonable access to NRMC records maintained by NR. NR shall cooperate with and, as requested, assist NRMC in the development, preparation and maintenance of all records and reports required by governmental authorities and related to NR's services hereunder.

7. Recordkeeping/Reporting. NR shall maintain financial records and reports, supporting documents, statistical records, and all other books, documents, papers or other records related and pertinent to this Agreement for a period of six (6) years from the date this Agreement expires or is terminated. If an audit, litigation or other action involving the records is started before the end of the four-year period, NR agrees to maintain the records until the end of the six-year period or until the audit, litigation or other action is completed, whichever is later.

8. Compliance with Applicable Law. In connection with the provision of services pursuant to this Agreement, NR agrees to comply with applicable Federal, state and local laws and regulations. ...

9. Independent Contractor Status. At all times during the operation of this Agreement, the parties shall be independent contractors with respect to each other and, except as described on Exhibit A, each party shall provide supervision of, and compensation for, its own employees, including the obligation to withhold appropriate amounts from employee compensation as required by law.

10. Default and Dispute Resolution Procedure. For purposes of this Agreement, "cause" shall be defined as the failure of either party to cure any material breach of this Agreement within thirty (30) days following receipt of a written notice of default from the other party. If a party believes that it has cause to terminate this Agreement or if the parties are unable to agree on annual amendments to Exhibit A, then the dispute shall be resolved as follows. Any and all Arbitrable Issues (as defined in this Section) shall be referred to a mutually agreeable independent third party. In such arbitration each party shall have the opportunity to provide written materials and present an oral summary of its position. The Arbitrator's decision in such arbitration shall be considered final, not appealable and binding upon the parties. Any dispute between the parties shall be deemed to be an "Arbitrable Issue" except a dispute in which a party reasonably and in good faith believes that its compliance with applicable governmental laws or regulations is at issue. Any dispute that is not an Arbitrable Issue shall be resolved by a court of competent jurisdiction or in such other manner as the parties may agree.

11. Notices. All notices, requests, demands and other communications required or permitted by this Agreement shall be in writing and shall be deemed to have been duly delivered if delivered in person or sent by registered or certified, first-class mail, postage prepaid, to the principal business address of the party to whom notice is given. Notice will be deemed effective upon delivery in person or three (3) days after mailing as required herein.

12. Amendment. This Agreement may be amended or modified only by a written instrument executed by both parties hereto.

13. Construction/Venue. This Agreement shall be construed, interpreted and enforced in accordance with the laws of the State of Delaware (without regard to conflicts of law provisions).

14. Binding Effect/Assignment. This Agreement shall be binding upon, and inure to the benefit of, the parties hereto and their respective successors and permitted assigns. Neither party hereto may delegate its duties nor assign its rights hereunder without the prior written consent of the other party.

THIS CONTRACT CONTAINS A BINDING ARBITRATION PROVISION WHICH MAY BE ENFORCED BY THE PARTIES.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

NEIGHBORHOOD
REINVESTMENT CORPORATION

By: _____

NEIGHBORHOOD RISK MANAGEMENT
CORPORATION

By: _____

Exhibit A Administrative Services Agreement

Scope of Services

Neighborwork® America may provide Neighborhood Risk Management Services with the following services under the direction of the Board of Directors of NRMC and the Chairperson of the appropriate Board committees:

1. Administrative services: including
 - a. Coordinating and attending Board meetings,
 - b. Providing communications and coordination to NRMC Board and members,
 - c. Coordination of financial record keeping,
 - d. Provide liaison with professional services, including audit and legal services.

2. Policy and product development:
 - a. Provide liaison with insurance consultants and assist in development of new programs and products,
 - b. Provide coordination with insurance agent on developing and implementing products and procedures,
 - c. Provide liaison with network for marketing,
 - d. Assist in development of risk management training and tools and to provide coordination with NeighborWorks® America Training Institute,
 - e. Assist NRMC in business planning.

Amendment No.2 to the
Administrative Services Agreement

This Amendment to the Administrative Services Agreement (the "Agreement") is made and entered into as of 2012, by and between Neighborhood Reinvestment Corporation, dba NeighborWorks America ("NW") and Neighborhood Risk Management Corporation ("NRMC"), a Delaware not-for-profit corporation.

WHEAREAS, NW and NRMC wish to amend Exhibit A to the Agreement; and

NOW THEREFORE, it is agreed by and between the parties as follows:

1. Amendment. Notwithstanding any other provision in the Agreement, including but not limited to Section 3, the parties hereby agree that the current Exhibit A to the Agreement is deleted in its entirety and replaced with the attached Exhibit A.
2. Non-Impairment. Except as expressly provided herein, nothing in this Amendment shall alter or affect any provision, condition, or covenant contained in the Agreement or affect or impair any rights, powers, or remedies provided by the Agreement, it being the intent of the parties that the provisions of the Agreement shall continue in full force and effect except as expressly modified hereby.
3. Counterpart Signatures. This Amendment may be signed in any number of counterparts, each of which shall be an original, with the same effect as if the signatures were upon the same instrument.

IN WITNESS WHEREOF, the parties have caused this Amendment to be signed and executed by those duly authorized persons indicated below, and their respective signatures constitute certification that each is authorized to execute and deliver this Amendment on behalf of the indicated party as of the date and year first above written.

NEIGHBORHOOD RISK MANAGEMENT CORP.

NEIGHBORWORKS AMERICA


BY: (Original version signed)

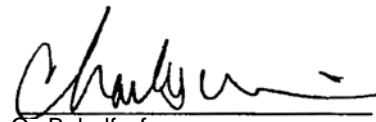
By: (Original version signed)

Exhibit A
NRMC Agreement

Scope of services from October 1, 2012 - - September 30, 2013

1. Goal: Support Transition. Neighborworks seeks to continue support of the transition to the permanent NRMC Executive Director ("ED") through the following:
 - a. Relate institutional history to ED.
 - b. Ensure the proper transfer of all NRMC files and records in the possession of NWA to ED.
2. Goal: Relationship Management Continuity: As NRMC has been an important tool to serve the network, NeighborWorks desires to remain connected to the work of NRMC and understand how NRMC can maintain its relevance and function for the network by:
 - a. Attending Board meetings and key committee meetings as NWA observer, when possible or when specifically requested.
 - b. Attending loss control meetings as NWA observer when possible or when specifically requested.
3. Goal: Communications: Recognizing that timely and accurate information is important for network members for the service provided by NRMC, to explore support options around NRMC's plan to generate communications to NWOs by:
 - a. Providing review and comment as requested to the NIAR Deputy Director, as NWA representative, to NRMC in development of marketing plan, responses to renewal related questions and other communications.
 - b. Examining methods that can support NRMC's communication plan to network members.
4. Goal: Advance Best Practices in Insurance and Risk Management: To establish a cooperative relationship on training between NRMC and NW:
 - a. Provide a Training liaison for NRMC relationship management around Training.


On Behalf of
Neighborhood Risk Management Corporation


On Behalf of
NeighborWorks America

W. Patrick Madden
Print Name

Chuck Wehzein
Print Name

Date 1/30/13

11/9/12