

OFFICE OF AUDIT
REGION 10
SEATTLE, WA



Gruening Park Apartments, Juneau, AK, Did Not Always Comply With HUD Rules and Regulations

2012-SE-1006

SEPTEMBER 5, 2012



U.S. DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT
OFFICE OF INSPECTOR GENERAL

Issue Date: September 5, 2012

Audit Report Number: 2012-SE-1006

TO: Renee D. Greenman, Director, Office of Housing – Multifamily Hub, 0AHM

//signed//

FROM: Ronald J. Hosking, Regional Inspector General for Audit, 0AGA

SUBJECT: Gruening Park Apartments, Juneau, AK, Did Not Always Comply With HUD Rules and Regulations

Enclosed is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our audit of Gruening Park Apartments' Section 236 and Section 8 programs in Juneau, AK.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8L, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 913-551-5870.



September 5, 2012

Gruening Park Apartments, Juneau, AK, Did Not Always Comply With HUD Rules and Regulations

Highlights

Audit Report 2012-SE-1006

What We Audited and Why

We audited Gruening Park Apartments (project), a 96-unit apartment complex in Juneau, AK, owned and operated by Alaska Housing Development Corporation, Inc. (owner), to determine whether the owner administered the project and its programs in compliance with the regulatory agreement and other HUD requirements. We selected this project primarily due to its having a significantly deficient surplus cash position of negative \$294,058.

What We Found

The owner generally administered the project and its programs in compliance with the regulatory agreement and other HUD requirements. However, it did not comply with HUD rules and regulations regarding its waiting list, security deposit collections, rent calculations, mortgage insurance premium payments, or management fee calculations. The owner made changes to the project's waiting list aimed at addressing our concerns and reimbursed the project for its overpaid management fees.

What We Recommend

We recommend that HUD require the owner to implement policies and procedures to improve its waiting list documentation, security deposit collections, recertification review process, and automatic withdrawals. We also recommend that the owner reimburse tenants for all overpayments, reconcile the mortgage insurance premium overpayment with the lender, and accurately calculate its management fee.

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BACKGROUND AND OBJECTIVE

Gruening Park Apartments

Gruening Park Apartments (project) is a 96-unit apartment complex in Juneau, AK. It is owned and operated by Alaska Housing Development Corporation, Inc. (owner), a nonprofit organization formed in 1972. The owner also owns the adjacent Eaglewood Apartments and Ravenwood Apartments. The U.S. Department of Housing and Urban Development (HUD) pays a portion of the project's mortgage interest expense under the Section 236 program. The project also has two Section 8 contracts that cover 56 units, and it converted one of the remaining units into its Neighborhood Networks Center. HUD authorized the project to retain its excess income to defray the Center's expenses. During our 2-year audit scope, HUD provided the project more than \$1.1 million between the two programs.

Section 236 – Interest Subsidy Payments

The Section 236 program provides interest reduction payments to the lender on behalf of the project. The interest reduction payments lower the project's operating costs and, in turn, the tenants' rent by bringing the effective mortgage rate down to 1 percent. Interest reduction payment amounts that exceed the interest due are retained by the project to cover other operating costs. A tenant must pay 30 percent of his or her adjusted income but no less than the basic rent established by HUD and no greater than the HUD-estimated fair market rent. Excess income is the amount of rent received above the basic rent. Section 236 rules apply to the entire project unless a more direct subsidy provides rental assistance, such as Section 8.

Section 8 – Housing Assistance Payments Program

The project-based Section 8 Housing Assistance Payments program provides rental assistance to low-income individuals and families, enabling them to live in affordable, decent, safe, and sanitary housing. HUD makes the assistance payment to the owner of an assisted unit on behalf of an eligible family, defined as having income at or below 80 percent of the area median income adjusted for family size. The tenant pays the higher of (1) 30 percent of his or her monthly adjusted income, (2) 10 percent of his or her monthly income, (3) welfare rent (if applicable), and (4) \$25 minimum rent. The project calculates the amount of the assistance payment, which is the difference between the contract rent and the tenant rent.

Our objective was to determine whether the owner administered the project and its programs in compliance with the regulatory agreement and other HUD requirements.

RESULTS OF AUDIT

Finding: The Owner Did Not Always Comply With HUD Rules and Regulations

The owner did not comply with HUD rules and regulations regarding its waiting list, security deposit collections, rent calculations, mortgage insurance premium payments, or management fee calculations. This noncompliance occurred because the owner lacked sufficient policies and procedures. As a result, the owner did not admit tenants appropriately, did not promptly refund security deposit overpayments, charged incorrect rent amounts, and overpaid its mortgage insurance premium escrow account and management fee.

The Waiting List Was Insufficient

The owner did not maintain an auditable waiting list. HUD Handbook 4350.3 states that owners must select applicants from the waiting list in chronological order. A notation must be made on the waiting list whenever an activity specific to an applicant occurs to provide an auditable record. Independent reviewers looking at the waiting list should be able to confirm that an applicant was appropriately housed. The owner, however, admitted some tenants ahead of others who applied before them, and the waiting list did not provide enough detail to justify these out-of-order selections.

The Owner Overcollected Security Deposits

The owner overcollected tenant security deposits. If a project elects to collect security deposits, HUD requires these deposits to equal, at most, 1 month's rent for Section 236 tenants and 1 month's total tenant payment for Section 8 tenants. Instead of reconciling deposits when paid, the owner reconciled the payments later and refunded any overpayments, sometimes as much as 2 years later.

The Owner Made Rent Calculation Errors

The owner made errors in calculating tenant rent. HUD Handbook 4350.3 requires the owner to correctly calculate rent and includes instructions for this calculation, including how to determine tenant income and incorporate contract rents. Despite reviewing each recertification, the owner made 10 different calculation errors in 7 of the 13 files sampled. These errors are described in appendix C.

The Owner Paid Excess Mortgage Insurance Premiums

The owner overpaid its mortgage insurance premiums. The regulatory agreement between HUD and the owner states that the owner may not pay out any funds except for reasonable operating expenses and necessary repairs. In addition, HUD created an amortization schedule that prescribed the amount the owner owed in principal, interest, and its mortgage insurance premium each month. The lender withdrew the funds from the project's operating account and placed the premiums in an escrow account. While the annual payments from the escrow account to the insurance fund followed the amortization schedule, the withdrawals from the project did not. The lender charged and withdrew higher monthly amounts associated with prior years on the amortization schedule, resulting in the owner's overpayment. These deviations from the schedule are shown in appendix D.

The Owner Incorrectly Calculated Management Fees

The owner based its management fee calculation on net rental income instead of rent receipts. HUD Handbook 4381.5 states that fees derived from project income must be calculated as a percentage of the income collected. The management certification shows that the owner agreed to manage the project for 6 percent of residential income collected. Instead of basing its calculation on rent receipts collected, the owner charged a management fee of 6 percent of net rental income earned.

In addition, the owner included excess income in net rental income. When HUD authorized the owner to retain excess income to fund its Neighborhood Networks Center, it required the owner to book the excess income separately from net rental income. Both this authorization and HUD Handbook 4381.5 also instructed the owner to exclude excess income collected when calculating the management fee. The owner, however, considered net rental income to be the appropriate amount on which to base its management fee calculation and included \$36,372 in excess income with net rental income. Since the owner based its management fee on net rental income, which was a different amount than income collected, it inappropriately included excess income in the calculation as well.

Policies and Procedures Were Insufficient

The project's policies and procedures were insufficient.

The waiting list documentation procedure was insufficient. Rather than making the required notations on the waiting list, the owner relied on staff members to remember applicant-specific activities. As a result of the audit, the owner made changes to its waiting list procedure to include the required notations, but the effectiveness of this new documentation method had not been tested.

The security deposit procedures did not prevent overcollection. The owner thought its reconciliation process was adequate and did not realize that periodic reimbursement of security deposits was not a satisfactory control.

The recertification review procedure was insufficient to ensure proper rent calculations. The owner did not have written policies and procedures for conducting a recertification. The owner thought its review process was adequate and was surprised to learn that it had made the calculation errors described in appendix C.

The owner also lacked procedures to ensure that mortgage payments followed the amortization schedule. The owner did not consider that the lender's charges would deviate from the amortization schedule, so it did not have a process to review these withdrawals to ensure that payments from the project's account were appropriate.

The owner lacked procedures to properly calculate management fees. After the owner received authorization to retain excess income, it thought it was allowed to treat excess income as rental income.

Errors Resulted From a Lack of Policies and Procedures

Due to the lack of sufficient policies and procedures,

- Six of thirteen tenants reviewed were housed out of order without appropriate justification;
- The owner did not promptly refund \$618 in overcollected security deposits, and some tenants went without hundreds of dollars for months, sometimes years;
- Three Section 8 tenants overpaid a total of \$2,146 in rent;
- A Section 236 tenant overpaid a total of \$204 in rent;
- Three Section 8 tenants underpaid a total of \$1,558 in rent;
- A Section 236 tenant underpaid a total of \$699 in rent;

- A Section 8 tenant did not receive \$114 in utility reimbursement;
- The owner unknowingly overpaid its mortgage insurance premium escrow account by \$2,171; and
- The owner paid itself \$2,304 in excess management fees. It repaid this amount as a result of the audit.

Recommendations

We recommend that the Director of Region X's Office of Multifamily Housing

- 1A. Review the owner's new waiting list procedure to ensure that it is auditable and effective.
- 1B. Require the owner to implement a procedure to prevent tenants from overpaying security deposits.
- 1C. Require the owner to improve its recertification review process to reduce rent calculation errors.
- 1D. Require the owner to reimburse tenants from nonproject funds for the \$2,350 in overpayments and the \$114 in unpaid utility reimbursement.
- 1E. Require the owner to reimburse HUD from nonproject funds for the \$1,558 in overpaid housing assistance resulting from Section 8 tenant underpayments.
- 1F. Require the owner to reimburse the project from nonproject funds for the \$699 in Section 236 rent underpayments.
- 1G. Require the owner to review all files outside our sample for similar calculation errors and reimburse tenants for any additional overpayments.
- 1H. Require the owner to reconcile the mortgage insurance premium overpayment with the lender.
- 1I. Require the owner to institute policies and procedures for reviewing automatic withdrawals.
- 1J. Require the owner to repay the project \$2,304 in excess management fees.¹
- 1K. Train the owner in the correct method of calculating its management fee to ensure that it is properly calculated in the future.

¹ The owner resolved this exception and reimbursed the project \$2,304. These funds would have been classified as ineligible had the issue not been resolved. Accordingly, we included that amount in appendix A, Schedule of Questioned Costs

SCOPE AND METHODOLOGY

Our audit period covered January 2010 through December 2011. We performed our fieldwork between April and June 2012 at the owner's office located at 1800 Northwood Drive, Juneau, AK.

To accomplish our objective, we reviewed applicable agreements, contracts, and HUD requirements; interviewed HUD and project staff; reviewed the project's policies and procedures; analyzed the project's financial statements and general ledger; examined the project's receipt and disbursement activity; reviewed the project's procurement of contracted services; analyzed the project's surplus cash, management fee, security deposits, and interest reduction payment revenue amounts; examined the project's reserve for replacement activity; and reviewed a sample of the project's tenant files.

Sample Selection

Of the project's 95 residential units, we reviewed the files pertaining to the 13 tenants living in 8 randomly selected units during our audit period. This nonstatistical sample was drawn using a random-number generator. This process yielded a mixture of Section 236 and Section 8 tenants, as well as a collection of units occupied by varying numbers of families during our audit period. The methodology for our review consisted of

1. Reviewing the file and the waiting list to determine whether the tenant was properly selected from the waiting list;
2. Reviewing the lease agreement to determine the tenant's security deposit and comparing it to the tenant deposit ledger and deposit receipts;
3. Completing a spreadsheet for each (re)certification using an Excel template that recreates the form HUD-50059 certification form;
4. Reviewing the file to determine whether (re)certifications were completed in a timely manner, the tenant met eligibility requirements, and the project obtained verifications for income and assets;
5. Reviewing the file to ensure that the owner calculated the correct housing assistance payment, utility assistance payment, and tenant rent as appropriate;
6. Reviewing the lease agreement to ensure that the contract rent was appropriate; and
7. Determining whether the owner properly admitted and recertified the tenant.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective:

- Controls to ensure proper selection from the waiting list.
- Controls to ensure that tenant security deposits complied with HUD requirements.
- Controls to ensure that rents and management fees were properly calculated.
- Controls to ensure that mortgage payments followed the amortization schedule.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The owner did not have adequate controls in place to ensure that tenants were properly selected from the waiting list (finding 1).
- The owner did not have adequate controls in place to ensure that tenant security deposits complied with HUD requirements (finding 1).

- The owner did not have adequate controls in place to ensure that rents and management fees were properly calculated (finding 1).
- The owner did not have adequate controls in place to ensure that mortgage payments followed the amortization schedule (finding 1).

APPENDIXES

Appendix A

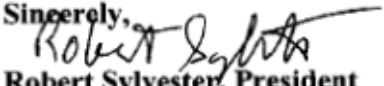
SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/
1D.	\$2,464
1E.	\$1,558
1F.	\$699
1J.	\$2,304

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.

Appendix B

AUDITEE COMMENTS

Alaska Housing Development Corporation	1800 Northwood Dr.
	Juneau, Ak. 99801
	(907) 780-6666
	(907) 780-4533 FAX
August 13, 2012	
Ronald J. Hosking, Regional Inspector General for Audit U.S. Department of Housing and Urban Development Office of Inspector General Office of Audit (Region 10) 909 First Avenue, Suite 126 Seattle, WA 98104	
Dear Mr. Hosking:	
Please find below Alaska Housing Development Corporation's (AHDC) written comments to the draft OIG report on Gruening Park Apartments, Juneau, Alaska. As requested these comments are being submitted in both hard and Word electronic copy.	
AHDC would like to thank the OIG staff for their time in reviewing our project. In general we agree with the findings outlined in the draft report. We also agree with the recommendations to implement additional policies and procedures to make improvements in several areas of our project management. These include our waiting list documentation, security deposit collection and reconciliation for applicable program requirements, internal recertification processing, reviewing automatic withdrawals by our Mortgagee for our annual mortgage insurance payment, and developing a procedure to make sure the management fee is accurately calculated.	
In closing, the Board of Directors and AHDC staff is committed to maintaining Gruening Park Apartments as a viable affordable housing resource in our community. Over the last 38 years of our relationship with the Department of Housing and Urban Development we have seen many changes in the rules and requirements for managing this property. We have always been willing to make changes and improvements in our management operations and thru this process we will continue to improve and strengthen our organization.	
If you have any questions, please contact Tamara Rowcroft, General Manager at (907) 780-4500.	
Sincerely,  Robert Sylvester, President Board of Directors	

Appendix C

TENANT RENT AND HUD ASSISTANCE CALCULATION ERRORS

The owner committed one or more of the following rent calculation errors in 7 of the 13 files reviewed:

- Omitted an eligible dependent deduction,
- Omitted a dependent's permanent fund dividend income,
- Miscalculated when annualizing income by averaging the wrong number of weeks,
- Based its calculations on the Section 8 contract rent for the unit instead of the market rent,
- Based its calculations on an outdated rent schedule,
- Inaccurately added child support payments,
- Failed to conduct an interim recertification in a timely manner,
- Used the amount of child support charged by the State rather than that received by the tenant,
- Included wage income from a position no longer held by the tenant, and
- Omitted the eligible portion of native corporation income.

The errors above resulted in the following overpayments and underpayments:

Family ID	Program	Rent OP	Rent UP	HAP OP	HAP UP	UR
2	Sec. 8	\$144	(\$1,272)	\$1,272	(\$144)	
8	Sec. 8	\$9			(\$9)	
10	Sec. 8		(\$270)	\$270		
11	Sec. 8		(\$16)	\$16		
12	Sec. 8	\$1,993			(\$2,107)	\$114
Sec. 8 Subtotal		\$2,146	(\$1,558)	\$1,558	(\$2,260)	\$114
6	Sec. 236	\$204				
7	Sec. 236		(\$699)			
Sec. 236 Subtotal		\$204	(\$699)			
Total		\$2,350	(\$2,257)	\$1,558	(\$2,260)	\$114

Key: ID – identification number
 Rent OP – rent overpaid by tenant to project
 Rent UP – rent underpaid by tenant to project
 HAP OP – rental assistance overpaid by HUD to project
 HAP UP – rental assistance underpaid by HUD to project
 UR – utility reimbursement

Appendix D

MORTGAGE INSURANCE PREMIUM OVERPAYMENTS

Month	Scheduled amount	Withdrawn amount	Overpayment amount
Jan-10	\$ 238.93	\$ 353.07	\$ 114.14
Feb-10	\$ 238.93	\$ 353.07	\$ 114.14
Mar-10	\$ 238.93	\$ 353.07	\$ 114.14
Apr-10	\$ 238.93	\$ 353.07	\$ 114.14
May-10	\$ 238.93	\$ 353.07	\$ 114.14
Jun-10	\$ 238.93	\$ 238.93	\$ 0.00
Jul-10	\$ 238.93	\$ 238.93	\$ 0.00
Aug-10	\$ 238.93	\$ 238.93	\$ 0.00
Sep-10	\$ 238.93	\$ 238.93	\$ 0.00
Oct-10	\$ 238.93	\$ 238.93	\$ 0.00
Nov-10	\$ 238.91	\$ 238.93	\$ 0.02
Dec-10	\$ 175.60	\$ 298.00	\$ 122.40
Jan-11	\$ 175.60	\$ 298.00	\$ 122.40
Feb-11	\$ 175.60	\$ 298.00	\$ 122.40
Mar-11	\$ 175.60	\$ 298.00	\$ 122.40
Apr-11	\$ 175.60	\$ 298.00	\$ 122.40
May-11	\$ 175.60	\$ 298.00	\$ 122.40
Jun-11	\$ 175.60	\$ 298.00	\$ 122.40
Jul-11	\$ 175.60	\$ 298.00	\$ 122.40
Aug-11	\$ 175.60	\$ 298.00	\$ 122.40
Sep-11	\$ 175.60	\$ 298.00	\$ 122.40
Oct-11	\$ 175.60	\$ 298.00	\$ 122.40
Nov-11	\$ 175.60	\$ 298.00	\$ 122.40
Dec-11	\$ 107.69	\$ 238.94	\$ 131.25
Total	\$4,843.10	\$7,013.87	\$2,170.77