Coconut Grove Apartments, Phoenix, AZ

Sections 223(f) and 241(a) Programs

Office of Audit, Region 9
Los Angeles, CA

Audit Report Number: 2015-LA-1008
September 22, 2015

To: Thomas Azumbrado, Director, San Francisco Multifamily Hub, 9AHMLAP

//SIGNED//

From: Tanya E. Schulze, Regional Inspector General for Audit, 9DGA

Subject: The Owner of Coconut Grove Apartments Did Not Always Operate Its HUD-Insured Project in Accordance With HUD Rules and Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Sections 223(f) and 241(a)-insured Coconut Grove Apartments multifamily project.

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 8M, 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 213-534-2471.

Audit Report Number: 2015-LA-1008
Date: September 22, 2015

The Coconut Grove Apartments' Owner Did Not Always Operate Its HUD-Insured Project in Accordance With HUD Rules and Requirements

Highlights

What We Audited and Why

We audited Coconut Grove Apartments due to concerns expressed by the U.S. Department of Housing and Urban Development's (HUD) Office of Multifamily Housing Programs regarding the management of the project. The main concern was that the owner may have diverted project funds for nonproject expenses. Our audit objective was to determine whether Coconut Grove's owner operated its Sections 223(f) and 241(a)-insured multifamily rental housing project in accordance with HUD rules and requirements.

What We Found

HUD's concerns about the project's management were valid. The owner did not always operate its multifamily project in accordance with HUD rules and requirements. Specifically, it recorded unsupported transactions that were charged to the project, and disbursed funds for non-HUD-approved rental credits and a loan to an employee. In addition, it did not obtain HUD approval for the management of the project. The owner failed to maintain an adequate financial management system and submit required financial statements to HUD and secured loans that placed unauthorized liens on the project. As a result, it did not ensure that at least $72,547 in unsupported transactions was used for eligible project expenses.

What We Recommend

We recommend that the Director of the San Francisco Office of Multifamily Housing Programs require the owner to (1) support or reimburse the project for the unsupported transactions and rental credits, (2) implement adequate written policies and procedures to address the finding cited in this report, and (3) obtain approval from HUD for its management.

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Background and Objective

The U.S. Department of Housing and Urban Development's (HUD) Section 223(f) program insures mortgage loans to facilitate the purchase or refinancing of multifamily rental housing. These projects may have been financed originally with conventional or Federal Housing Administration (FHA)-insured mortgages. Properties requiring substantial rehabilitation are not eligible for mortgage insurance under this program. HUD requires completion of critical repairs before endorsement of the mortgage and permits the completion of noncritical repairs after the endorsement for mortgage insurance. This program insures lenders against loss on mortgage defaults.

HUD's Section 241(a) program insures mortgage loans to finance repairs, additions, and improvements to multifamily rental housing and health care facilities with FHA-insured first mortgages or HUD-held mortgages. This program insures lenders against loss on mortgage defaults. It is intended to keep the project competitive, extend its economic life, and finance the replacement of obsolete equipment.

Tuscan Grove Properties, LLC, owns Coconut Grove Apartments, a 236-unit multifamily rental housing project located in Phoenix, AZ. In December 2005, HUD executed regulatory agreements with the owner in which the owner agreed to be bound by the terms and conditions of the agreements for two mortgage loans insured by FHA. Specifically, the owner assumed a more than $3.4 million acquisition loan and a $438,200 supplemental loan for project improvements under Sections 223(f) and 241(a) of the National Housing Act, respectively. In addition, the owners executed agreements with HUD that released the previous owner from all liability for obligations and responsibilities.

Our audit objective was to determine whether Coconut Grove's owner operated its Sections 223(f) and 241(a)-insured multifamily rental housing project in accordance with HUD rules and requirements.

Results of Audit

Finding: Coconut Grove Apartments' Owner Did Not Always Operate Its HUD-Insured Project in Accordance With HUD Rules and Requirements

Coconut Grove Apartments' owner did not always operate its HUD-insured project in accordance with HUD rules and requirements. Specifically, the owner (1) recorded unsupported transactions that were charged to the project, (2) failed to obtain HUD approval for the use of rental credits, (3) disbursed funds for a loan without a surplus cash flow, (4) failed to obtain HUD approval for its management, (5) failed to maintain an adequate financial management system, (6) failed to submit required financial statements to HUD, and (7) secured loans that placed unauthorized liens on the project. These conditions occurred because the owner generally lacked an understanding of HUD's rules and requirements in relation to the financial aspects of the project and disregarded HUD's rules and requirements in relation to the management of the project. In addition, the owner lacked written policies and procedures to ensure project compliance. As a result, it did not ensure that at least $72,547 in unsupported transactions was used for eligible project expenses.

Unsupported Transactions

The owner recorded $54,873 in unsupported transactions that were charged to the project. This amount included $36,000 in accounting journal entries, $14,873 in expenses, and $4,000 related to a deposit.

The Owner Lacked Documents To Support Accounting Journal Entries

Coconut Grove's regulatory agreements, sections 9(c) and 9(d), require its owner to keep the books and accounts of the operations in condition for a proper audit and in accordance with HUD requirements (see appendix C). The owner's general ledger showed three accounting journal entries, each in the amount of $12,000 that had a corresponding entry monetarily canceling it out. However, there were no records to support the three journal entries totaling $36,000 (see appendix D). As a result, the owner recorded journal entries for $36,000 in unsupported transactions.

The Owner Made Unsupported Disbursements

Coconut Grove's regulatory agreements, section 6(b), prohibit using program funds, except for reasonable operating expenses or necessary repairs, unless it is from surplus cash. Additionally, HUD Handbook 4370.2, REV-1, paragraph 2-6(E), requires that all disbursements from the regular operating account be supported by approved invoices or bills or other supporting documentation (see appendix C). The owner disbursed up to $14,873 for unsupported expenses (see appendix D). Of this amount, it disbursed $12,688 to a related intercompany bank account for unsupported payroll expenses. The owner disbursed $2,185 to individuals, including employees, for unsupported purposes or services. It could not support these expenses with invoices, bills, or other supporting documentation.

The Owner Made an Unsupported Deposit

Contrary to Coconut Grove's regulatory agreements, sections 9(c) and 9(d) (see appendix C), the owner's general ledger and bank statements showed an unsupported deposit of $4,000 (see appendix D). The property manager explained that the deposit was a loan that Coconut Grove received. However, the owner did not provide supporting documents for the loan or show that it properly recorded the loan in its general ledger. In addition, the owner's trial balances did not support that the transaction had been recorded.

Failure To Obtain HUD Approval for Use of Rental Credits

Coconut Grove's regulatory agreements, section 6(h), prohibit the use of dwelling accommodations without HUD approval for any purpose, except that which was originally intended. From November 2011 through May 2015, the project had at least two non-revenue-generating rental housing units that were occupied by individuals who were provided monthly rental credits (see appendix D). According to Coconut Grove's property manager and owner, monthly employee concessions, or rental credits, were given to individuals who worked at the project. However, the owner did not obtain HUD approval for the use of rental credits. The owner was not aware of the requirement for HUD approval of employee concessions. It stated that it would correct this noncompliance. The amount of lost rental revenue for the two non-revenue-generating rental housing units and individuals totaled at least $17,674.

Loans to Employees Without Surplus Cash

Coconut Grove's regulatory agreements, section 6(b), prohibit using program funds, except for reasonable operating expenses or necessary repairs, unless it is from surplus cash. The owner loaned project funds from its regular operating account without determining the availability of surplus cash. The owner provided $1,875 in payroll advances to employees. Currently, the owner deducted $1,675 from the employees' pay to repay the loaned funds. There is still an outstanding loan amount of $200 owed to the project from an employee. This amount is included in the reported unsupported disbursements that totaled $14,873. While the employees repaid most of the loans, the owner should not have used project funds for nonproject activities unless paid from surplus cash.

Failure To Obtain HUD Approval for Management

Coconut Grove's regulatory agreements, section 6(c), prohibit the owner from conveying, assigning, or transferring any right to manage the project without HUD approval. Further, HUD Handbook 4381.5, REV-2, section 2-6, requires that a management agent, including the owner, assume management responsibility of the project only after HUD approval and the following actions: the execution and submission of the appropriate certification form and the execution of a management agreement. The owner did not have the required HUD approvals, certification forms, or agreements to self-manage or convey project management rights to its identity-of-interest management agent, Optima Management Services, LLC. Since August 2006, the owner appeared to have self-managed the project. As of January 2013, Optima Management Services, LLC, managed the project without compensation.

The owner claimed it was not aware that it needed HUD approval to self-manage the project. However, HUD project files showed that the owner was aware of the requirement. In November 2005, the owner obtained approval for, executed, and submitted the required management documents for its last HUD-approved management agent. These management documents included the owner's certification (form HUD-9839-B) certifying that it would submit a new management agent certification to HUD before making changes in the project's management, including undertaking self-management of the project. In March 2006, the owner certified that the management certification and agent approval topics were discussed at loan closing. Additionally, emails, dated February and November 2007 and October 2009, noted that the subject of management approval was discussed by HUD and the owner. For example, the email, dated October 2009, included details about the documents needed to obtain HUD approval for a management agent. This email included HUD form numbers and referenced HUD Handbook 4381.5, REV-2, as a guide to help the owner obtain an approved management agent. In October 2007 and July 2011, HUD communicated through official letters to the owner about violations of the executed regulatory agreements, which included the required approval for a management agent. Thus, the owner disregarded the requirements for obtaining approval for the project's management.

Inadequate Financial Management System

Coconut Grove's regulatory agreements, sections 9(c) and 9(d), require its owner to keep the books and accounts of the operations in condition for a proper audit and in accordance with HUD requirements. HUD Handbook 4370.2, REV-1, CHG-1, paragraph 2-3(B) and section 2-4, require that financial records be complete, accurate, and updated monthly. Chapter 4 defines the prescribed uniform system of accounts used by owners of all HUD-insured properties. The owner did not have a financial management system that complied with its regulatory agreements or HUD's handbook. Specifically,

- It did not maintain a complete and accurate general ledger of its transactions. At least 32 percent of the general ledger line item records did not have reference numbers to identify project transactions. The property manager explained that the project management software, Rent Manager, did not assign reference numbers to electronic check (online payment) transactions and that the bookkeeper did not enter reference numbers into these fields. Therefore, the reference number fields for these transactions were left blank.

- It did not use HUD's prescribed uniform system of accounts with account categories that followed generally accepted accounting principles. Coconut Grove's trial balances and profit and loss statements for the periods ending December 31, 2013 and 2014, and March 31, 2015, had discrepancies in the income statement accounts balances as well as missing accounts. The property manager explained that the recording and classification of the project's accounting transactions were performed using Rent Manager's preset chart of accounts, that had inconsistencies related to misclassified accounts.

- It lacked procedures to manage the project's operations. For example, it did not have written policies and procedures or management contracts that defined roles, qualifications, or duties. In addition, it did not have written accounting policies and procedures to ensure compliance with HUD rules and requirements.

Required Financial Statements Not Submitted to HUD

Coconut Grove's regulatory agreements, section 9(e), require that the owner submit audited annual financial statements within 60 days following the end of each fiscal year. HUD regulations at 24 CFR (Code of Federal Regulations) 5.801(c)(2) allowed HUD to extend the time to submit the documents from 60 to 90 days. Since its fiscal year ending December 31, 2011, the owner had not submitted its financial statements to HUD. In May 2015, it stated that the financial statements for the fiscal year ending December 31, 2011, were complete and waiting to be signed by the certified public accounting firm. About 3½ years later, in June 2015, the owner submitted these financial statements to HUD. In May 2015, it provided a signed engagement letter related to the financial statements for the fiscal year ending December 31, 2012. The engagement letter was dated a week after the start of our review in April 2015. Overall, the owner explained that the filing of the financial statements was delayed due to personal medical issues that caused delays in providing requested documents to the certified public accountant responsible for ensuring that audited financial statements were submitted to HUD before the deadlines. The owner did not respond to our requests for additional information related to Coconut Grove's action plan to comply with HUD's requirements regarding the submission of its financial statements for the fiscal years ending December 31, 2012, 2013, and 2014.

Unauthorized Liens on the Project

Coconut Grove's regulatory agreements, section 6(c), prohibit the owner from conveying, assigning, or transferring any beneficial interest in any trust holding title to the project or receiving the rents and profits from the project without HUD approval. The owner secured two loans recorded by the Maricopa County Recorder's Office that placed unauthorized liens on the project without HUD approval. HUD was unaware of the owner's actions until April 2015. In April 2007, the owner placed the first lien on the project related to a $3 million loan. In November 2008, the lender released the owner from this debt and transferred the project title back to the owner. In June 2013, the owner placed a second lien on the project that remained active. This lien did not contain the details of the related loan, including the loan amount. The owner had not provided documentation related to the second lien. However, on August 20, 2015, the owner provided documentation that showed the lien being terminated on June 5, 2015. As a result, this issue has been resolved.

Conclusion

The owner of Coconut Grove did not always operate its HUD-insured project in accordance with HUD rules and requirements. This condition occurred because the owner did not understand the rules and requirements related to the financial aspects of the project, disregarded rules and requirements related to the management of the project, and lacked written policies and procedures to ensure project compliance. As a result, the project incurred at least $72,547 in unsupported project expenses, and the owner's practices confirmed HUD's concerns about the owner's use of project funds for nonproject expenses.

Recommendations

We recommend that the Director of HUD's San Francisco Office of Multifamily Housing Programs require the owner to

1A. Provide supporting documentation for the $36,000 in unsupported accounting journal entries and correct inaccurate information related to these entries in its general ledger.

1B. Provide supporting documentation for the $14,873 in unsupported disbursements that included a $200 loan to an employee, or repay its project from nonproject funds for costs that remain unsupported.

1C. Provide supporting documentation for the $4,000 unsupported loan deposit entry and correct inaccurate information related to the deposit in its general ledger.

1D. Obtain written approval from HUD for the $17,674 in unsupported rental credits or repay its project from nonproject funds for rental credits that remain unsupported.

1E. Develop and implement written policies and procedures to ensure that project funds are used solely for reasonable operating expenses or necessary repairs unless it receives prior written approval from HUD and uses surplus cash.

1F. Obtain written approval from HUD for its management agent and execute a management agreement that defines the management agent's roles and responsibilities as required by HUD rules and requirements.

1G. Develop and implement written policies and procedures to address the financial operations of the project.

1H. Submit to HUD all outstanding financial statements.

1I. Obtain HUD training and technical assistance for itself and its identity-of-interest management agent to ensure compliance with HUD rules and requirements that pertain to the management and operation of its project.

Scope and Methodology

We performed our audit work at Coconut Grove's office in Phoenix, AZ, and our offices in Phoenix, AZ, and Los Angeles, CA, from April 20 to June 26, 2015. Our review generally covered the period January 1, 2013, to March 31, 2015, and was expanded as necessary.

To accomplish our objective, we performed the following:

- Obtained relevant background information;
- Reviewed the regulatory agreements and applicable HUD rules, regulations, and guidance;
- Reviewed Coconut Grove's owner's articles of organization;
- Reviewed Coconut Grove's owner's fiscal year 2010 audited financial statements;
- Reviewed Coconut Grove's general ledger;
- Reviewed bank statements related to income deposits and expenditures;
- Interviewed Coconut Grove's owner and staff; and
- Interviewed HUD Phoenix Office of Multifamily Housing Programs staff.

The audit universe consisted of deposits and expenses totaling more than $2.14 and $2.15 million, respectively, during the period January 1, 2013, through March 31, 2015. For our review, we nonstatistically sampled 67 transactions totaling $98,115 in deposits, $290,759 in expenses, $36,000 in journal entries that resulted in the transactions monetarily canceling out, and a $400 voided check. Overall, the deposits and expenses reviewed represented 5 percent ($98,115/$2,143,462) and 14 percent ($290,759/$2,153,578) of the total deposits and expenses, respectively.

We relied in part on Coconut Grove's general ledger as a basis for defining the audit universe and selecting a sample for testing. Using the data analysis application ACL Analytics, we analyzed Coconut Grove's general ledger and determined that it was sufficiently reliable to meet the audit objective and for the intended use of the data.

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(s). We believe that the evidence obtained provides a reasonable basis for our findings 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:

- Effectiveness and efficiency of operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

- Reliability of financial information – Policies and procedures that management has implemented to reasonably ensure that it obtains relevant and reliable information to adequately support program expenditures and discloses that information in the required reports.

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that program expenses are supported and comply with program funding guidelines and restrictions.

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 project did not have adequate controls over program operations to ensure project management by a HUD-approved management agent (see finding).

- The project did not have an adequate financial management system and controls to ensure that the project's books and records were maintained in accordance with HUD requirements (see finding).

Appendixes

Appendix A

Schedule of Questioned Costs

Recommendation number	Unsupported 1/
1A	$36,000
1B	$14,873
1C	$4,000
1D	$17,674
Totals	**$72,547**

1/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation | **Auditee Comments**

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August 20, 2015

Via Email to: tschulze@hudoig.gov
Copies Via First Class U.S. Mail

Ms. Tanya E. Schulze
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
611 West Sixth Street
Suite 1160
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Re: Owner's additional information for and Response to draft Audit Report No. 2015 – LA – 100X, dated July XX, 2015 (cover letter dated July 31, 2015) (the "Draft Audit Report") regarding Coconut Grove Apartments, a 236-unit multifamily rental housing project located at 2028 West Indian School Road, Phoenix, Arizona 85015 (the "Project"), owned by Tuscan Grove Properties, LLC, an Arizona limited liability company ("Owner"), having an address at 6040 East Main Street, #466, Mesa, Arizona 85205

Dear Ms. Schulze:

Comment 1

This will acknowledge receipt, on or about August 3, 2015, of a copy of the Draft Audit Report. This will also acknowledge and thank you for the exit conference meeting (the "Exit Meeting") held August 14, 2015 at 10:00 a.m., local time, in Phoenix, Arizona at which the Draft Audit Report was discussed with Owner representatives and counsel. Please be advised that this letter is to provide you and the U.S. Department of Housing and Urban Development ("HUD") with additional information and supportive documentation for questions/issues raised in the Draft Audit Report, as well as certain written comments to the Draft Audit Report on behalf of the Owner.

Comment 2

Please be advised that this firm and the undersigned are acting as counsel for Owner and the Project. Your consideration of the attached information and comments prior to finalizing the Draft Audit Report will be most appreciated.

Comment 3

Initially, as we advised those present during the Exit Meeting, the two mortgage loans (the "Existing Mortgage Loans") assumed by Owner on its acquisition of this Project constitute

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Tanya E. Schulze
August 20, 2015
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Owners first experience with loans insured by the Federal Housing Administration ("FHA") under HUD's Sections 223(f) and 241(a) programs. Owner continues to get used to the many applicable HUD rules and regulations and looks forward to working with HUD to correct or resolve remaining issues as to compliance with HUD's rules and regulations after your consideration of Owner's comments in this response letter.

Comment 4

Further, we note and call to your attention, to the attention of our lenders under the Existing Mortgage Loans, to our residents at the Project, to the resident referral agencies with whom we work and to other regulatory agencies that the unresolved issues found in the Draft Audit Report: (a) are relatively minor in scope and amount, primarily relate to certain unique bookkeeping and management requirements imposed by HUD (such as, for example, the requirement to establish a surplus cash flow before allowing rent credits for on-site maintenance engineers); (b) do not reflect any defaults under the Existing Mortgage Loans (i.e., all loan payments have been and continue to be timely made); (c) are generally correctible upon updating of the Project's financial management system and presentation of documentation supporting questioned journal entries, or seeking and obtaining HUD approval for such things as use of rental credits and management of the Project by Owner; and (d) completion and presentation to HUD of certain outstanding financial statements. Those items not corrected pursuant to this letter are being diligently worked upon and we anticipate any such remaining items will be corrected shortly in cooperation with and with guidance from the local Phoenix HUD office.

Comment 5

We emphasize that the Project and Owner are making their loan payments and other obligations as they become due and are operating the Project in a clean and orderly fashion consistent with industry standards in the area.

Comment 6

To address the stated results of the Draft Audit Report, we provide and attach hereto supporting documents and/or or explanatory information to support transactions or items initially found to be inadequate or questionable:

Sincerely,

FENNEMORE CRAIG, P.C.

Don J. Miner

Don J. Miner

DMIN

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OIG Evaluation of Auditee Comments

Comment 1 We appreciate the owner's acknowledgement of the report and the opportunity to meet with the owner to discuss the report.

Comment 2 We acknowledge that Fennemore Craig will be the legal counsel for the owner.

Comment 3 We acknowledge the circumstances that the owner experienced in operating its only HUD-insured property. We commend the owner for taking the necessary corrective actions to ensure compliance with HUD rules and requirements. Further, we believe that the implementation of the recommendations in this report will help the owner be in compliance with HUD rules and requirements.

Comment 4 We appreciate the owner's acknowledgement of the issues identified in this report. For clarification, establishing the availability of surplus cash allows for the disbursement of advances to project employees. In addition, HUD approval is necessary before the owner can provide rent credits to on-site maintenance engineers. During the audit resolution process, the owner will have the opportunity to provide HUD documentation to support the rent credits in question.

Comment 5 We commend the owner for being current on its mortgage payments. We appreciate the owner for taking the necessary corrective actions to ensure compliance with HUD rules and requirements.

Comment 6 We appreciate the owner for providing us supporting documentation for review. The owner provided supporting documentation to support that the second lien on the project was terminated on June 5, 2015. Additionally, the owner provided supporting documentation for $5,524 in disbursements made to individuals and for security expenses. This supporting documentation showed that the owner had loaned an additional $1,375 of project funds from its regular operating account without determining the availability of surplus cash. As a result, the owner provided $1,875 in loans to employees. The owner provided documentation to support the deduction of $1,675 from the employees' pay towards the loaned funds. There is still one employee who owes the project $200. As a result, we reduced the $20,397 in reported unsupported transactions to $14,873 and revised the total loans made to employees without determining surplus cash from $500 to $1,875.

The owner provided insufficient supporting documentation for the $36,000 in unsupported journal entries identified in the report. Instead, the owner provided general ledger accounting summaries for each of the questioned unsupported journal entries. The general ledger accounting summaries show accrued payroll expenses for contracted employees. However, the documentation did not show that the liabilities related to these expenses were recorded or that reversal entries were made once the expenses were paid. During the fieldwork, the owner did not provide a contract for “leased” employees identified in the documentation. As a result, the $36,000 in questioned accounting journal entries is still unsupported.

The owner provided insufficient supporting documentation for the reported $4,000 unsupported loan deposit entry. The owner provided a transfer history report dated August 20, 2015, that scheduled a transfer of $4,000 to the bank account from where the loaned funds were obtained. In addition, the owner provided a copy of an e-mail from the bank stating that the capability to perform intercompany transfers using the project bank account were to be removed. However, the owner did not provide a copy of the confirmation that showed the complete transfer of questioned funds. Consequently, the questioned $4,000 loan deposit entry is still unsupported.

Based on our review of the documentation, we adjusted the report accordingly. Furthermore, copies of the supporting documentation are not included within this report, but are available upon request. As previously stated, the owner will have the opportunity to work with the HUD Office of Multifamily Housing Programs to resolve the remaining issues identified in the report.

Appendix C

Criteria

The following sections of the regulatory agreements; 24 CFR Part 5; Handbook 4370.2, REV-1, CHG-1; and Handbook 4381.5, REV-2, were relevant to our audit of Coconut Grove Apartments.

Regulatory Agreements, Section 6
Owners shall not without the prior written approval of the Secretary:

(b) Assign, transfer, dispose of, or encumber any personal property of the project, including rents, or pay out any funds except from surplus cash, except for reasonable operating expenses and necessary repairs.

(c) Convey, assign, or transfer any beneficial interest in any trust holding title to the property, or the interest of any general partnership owning the property, or any right to manage or receive the rents and profits from the mortgaged property.

(h) Permit the use of the dwelling accommodations or nursing facilities of the project for any purpose except the use which was originally intended, or permit commercial use greater than that originally approved by the Secretary.

Regulatory Agreements, Section 9
(c) The mortgaged property, equipment, buildings, plans, offices, apparatus, devices, books, contracts, records, documents, and other papers relating thereto shall at all times be maintained in reasonable condition for proper audit and shall be subject to examination and inspection at any reasonable time by the Secretary or his duly authorized agents. Owners shall keep copies of all written contracts or other instruments which affect the mortgaged property, all or any of which may be subject to inspection and examination by the Secretary or his duly authorized agents.

(d) The books and accounts of the operations of the mortgaged property and of the project shall be kept in accordance with the Requirements of the Secretary.

(e) Within sixty (60) days following the end of each fiscal year the Secretary shall be furnished with a complete annual financial report based upon an examination of the books and records of mortgagor prepared in accordance with the requirements of the Secretary, prepared and certified to by an officer or responsible Owner and, when required by the Secretary, prepared and certified by a Certified Public Accountant, or other person accept able to the Secretary.

24 CFR Part 5, General HUD Program Requirements; Waivers, Section 5.801, Uniform financial reporting standards

(c) *Filing of financial reports.* (2) For entities listed in paragraphs (a)(3) and (4) of this section, the financial information to be submitted to HUD in accordance with paragraph (b) of this section, must be submitted to HUD annually, no later than 90 days after the end of the fiscal year of the reporting period, and as otherwise provided by law.

Handbook 4370.2, REV-1, CHG-1: Financial Operations and Accounting Procedures for Insured Multifamily Projects, Chapter 2, Section 2-3: Maintenance of Books and Accounts

(b) Books and accounts must be complete and accurate. The books of original entry must be kept current at all times, and postings must be made at least monthly to ledger accounts. Standard journal entries may be established for recurring items and posted monthly.

Handbook 4370.2, REV-1, CHG-1: Financial Operations and Accounting Procedures for Insured Multifamily Projects, Chapter 2, Section 2-4: Prescribed Accounts

In order to ensure that books are complete and reporting is uniform, prescribed accounts must be maintained as outlined and described in Chapter 4.

Handbook 4370.2, REV-1, CHG-1: Financial Operations and Accounting Procedures for Insured Multifamily Projects, Chapter 2, Section 2-6: Regular Operating Account

(e) All disbursements from the Regular Operating Account (including checks, wire transfers and computer generated disbursements) must be supported by approved invoices/bills or other supporting documentation. The request for project funds should only be used to make mortgage payments, make required deposits to the Reserve for Replacements, pay reasonable expenses necessary for the operation and maintenance of the project, pay distributions of surplus cash permitted and repay owner advances authorized by HUD.

Handbook 4370.2, REV-1, CHG-1: Financial Operations and Accounting Procedures for Insured Multifamily Projects, Chapter 4: HUD Chart of Accounts, Section 4-1: Introduction

This chapter lists and defines the prescribed uniform system of accounts used by owners of all HUD-insured projects. To assure that project accounting transactions are properly recorded and classified, project bookkeepers must familiarize themselves with the account definitions contained in this chapter.

Handbook 4381.5, REV-2, Chapter 2: Approval of Management Agents, Section 2.6: Management Agent Assumption of Responsibility

Generally, the management agent may assume management responsibility only after:

(a) The HUD Loan/Asset Management staff has issued a letter approving the agent proposed by the owner; and

(b) The owner and agent have executed and submitted the appropriate Management Certification form (Form HUD-9839a, b, or c); and

(c) The owner and agent have executed a Management Agreement, as necessary.

Appendix D

Summary of Questioned Costs

Date	Reference number	Description	Amount
8/20/2013	J3801	Journal entry	$12,000
10/20/2013	J3802	Journal entry	$12,000
11/20/2013	J3803	Journal entry	$12,000
Total of unsupported journal entries			**$36,000**
4/5/2013	J2880	Disbursement for payroll	$12,688
10/21/2013	109508	Disbursement to individual	$595
11/14/2013	109511	Disbursement to individual – payroll advance	$200
3/6/2014	109537	Disbursement to individual	$595
5/1/2014	109546	Disbursement to individual	$595
5/27/2014	109548	Disbursement to individual	$200
Total of unsupported disbursements to individuals and for payroll and security expenses			**$14,873**
4/22/2014	J3270	Loan	$4,000
Total of unsupported loan			**$4,000**

Questioned rental credits

Month	Amount
November 2011	$416
December 2011	$558
February 2012	$408
March 2012	$408
April 2012	$408
May 2012	$405
June 2012	$405
August 2012	$408
September 2012	$408
October 2012 - March 2015 (30 months x $400 per month)	$12,000
April 2015	$925
May 2015	$925
Total	**$17,674**