



# Morris Park Nursing and Rehabilitation Center, Bronx, NY

## Section 232 HUD-Insured Loan Program



**To:** Roger Lewis, Director, Office of Residential Care Facilities, HP  
**//SIGNED//**

**From:** Kimberly Greene, Regional Inspector General for Audit, 2AGA

**Subject:** Morris Park Did Not Always Comply With Its Regulatory Agreement and HUD 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 Morris Park Nursing and Rehabilitation Center's Section 232 HUD-insured loan program.

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 212-264-4174.



**Audit Report Number: 2015-NY-1012**

**Date: September 30, 2015**

**Morris Park Did Not Always Comply With Its Regulatory Agreement and HUD Requirements**

## Highlights

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### What We Audited and Why

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We audited Morris Park Nursing and Rehabilitation Center based on a risk assessment we performed on nursing homes located in New York and New Jersey. Morris Park has a Section 232 HUD-insured loan in the amount of \$7.4 million. The objective of the audit was to determine whether Morris Park officials managed funds in compliance with the regulatory agreement and applicable HUD requirements.

### What We Found

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Morris Park officials generally managed funds in accordance with the regulatory agreement and HUD requirements. However, in 2013 and 2014, they made two \$60,000 distributions to the nursing home's owner, 1235 Pelham Parkway Realty, LLC, in violation of the regulatory agreement. In addition, officials did not perform monthly reconciliations of accounting records and submit audited financial statements in a timely manner. These conditions occurred because nursing home officials were not aware of all necessary requirements, compliance with HUD requirements was not emphasized, and accounting procedures were not documented. As a result, nursing home officials could not ensure that the distributions complied with the regulatory agreement, accounting records were reconciled monthly, and audited financial statements were provided in a timely manner.

### What We Recommend

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We recommend that the Director of HUD's Office of Residential Care Facilities instruct nursing home officials to (1) establish and implement procedures requiring any distributions to the owner to comply with the regulatory agreement and HUD requirements, (2) establish and implement written accounting procedures to ensure that books and records are maintained in accordance with HUD requirements, (3) ensure that accounting records are reconciled monthly, and (4) implement procedures to ensure the timely preparation of audited financial statements.

# Table of Contents

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<b>Background and Objective.....</b>	<b>3</b>
<b>Results of Audit .....</b>	<b>4</b>
<b>Finding: Morris Park Did Not Always Comply With Its Regulatory Agreement     and HUD Requirements .....</b>	<b>4</b>
<b>Scope and Methodology.....</b>	<b>7</b>
<b>Internal Controls.....</b>	<b>9</b>

# Background and Objective

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Morris Park Nursing and Rehabilitation Center is a 191-bed skilled nursing facility that provides 24-hour comprehensive inpatient care to adults of all ages. The nursing home is located at 1235 Pelham Parkway North, Bronx, NY. The nursing home's owner, 1235 Pelham Parkway Realty, LLC, is a limited liability company that received a Section 232 U.S. Department of Housing and Urban Development (HUD)-insured loan. The \$7.4 million loan was endorsed on July 8, 2009, and has an unpaid principal balance of \$6.4 million. The maturity date for the loan is August 1, 2034, with monthly debt service of \$43,883.

HUD's Office of Residential Care Facilities administers the Section 232 loan program. Section 232 is a Federal Housing Administration-insured loan product that covers housing for the frail elderly and those in need of supportive services. Nursing homes, assisted living facilities, and board and care facilities are examples of Section 232 housing. This loan program may be used to finance the purchase, refinance, new construction, or substantial rehabilitation of a project.

Section 232 requires that all owners and operators execute a regulatory agreement. This agreement is intended to govern the operation of the project. At closing, the regulatory agreement is recorded and is in effect throughout the period in which HUD is the owner, holder, or insurer of the note. Owners and operators are responsible for any violations of the regulatory agreement and may be subject to adverse actions if they occur. The regulatory agreement requires that books, records, and contracts be maintained in reasonable condition for proper audit and examination at all times.

We provided Morris Park officials with the discussion draft report on August 24, 2015, and they declined to provide written comments before and at the September 17, 2015, exit conference. Morris Park officials generally agreed with the finding and indicated that they would implement the recommendations.

The objective of the audit was to determine whether Morris Park officials managed funds in compliance with the regulatory agreement and applicable HUD requirements.

# Results of Audit

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## **Finding : Morris Park Did Not Always Comply With Its Regulatory Agreement and HUD Requirements**

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Morris Park officials generally managed funds in accordance with the regulatory agreement and HUD requirements. However, in 2013 and 2014, they made two \$60,000 distributions to the nursing home's owner, 1235 Pelham Parkway Realty, LLC, in violation of the regulatory agreement. In addition, they did not perform monthly reconciliations of accounting records and submit audited financial statements in a timely manner. These conditions occurred because nursing home officials were not aware of all necessary requirements, compliance with HUD requirements was not emphasized, and accounting procedures were not documented. As a result, nursing home officials could not ensure that the distributions complied with the regulatory agreement, accounting records were reconciled monthly, and audited financial statements were provided in a timely manner.

### **Unallowable Distributions Were Made**

In 2013 and 2014, Morris Park officials made two \$60,000 distributions to the owner in violation of the regulatory agreement.<sup>1</sup> In January 2012, HUD's Real Estate Assessment Center notified the owner that Morris Park had health and safety violations that required correction and it had received an inspection score of 26c.<sup>2</sup> The owner filed an appeal with the Real Estate Assessment Center, and although the inspection score had increased to 55, it was below the required passing score of 60. In April 2015, HUD's Departmental Enforcement Center notified the owner that the distributions should not have been made. The owner's regulatory agreement, section 6(e)(4), states that owners must not make or receive and retain any distribution of assets or any income of any kind from the project except surplus cash and only when there is compliance with all outstanding notices of requirements for proper maintenance of the project. During our audit, nursing home officials stated that they were not aware of the distribution requirements in the regulatory agreement. As a result, HUD could not ensure that the distributions to the owner complied with the regulatory agreement.

On June 3, 2015, during our audit, both distributions totaling \$120,000 were repaid by the owner. We obtained the nursing home inspection report to determine whether the health and safety violations had been corrected. One of the deficiencies listed in the report stated that patient alert systems located beside beds were inoperable for 18 units inspected. We conducted a limited review by inspecting patient alert systems in 6 of the 18 units and determined that all were in operating condition. Additionally, nursing home officials stated that all deficient items in the inspection report had been corrected. The Departmental Enforcement Center requested

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<sup>1</sup> Distributions to owners may be made when there is surplus cash and when the nursing home receives an inspection score of 60 or above from a possible 100.

<sup>2</sup> The lowercase letter "c" is given if one or more exigent or fire safety issues call for immediate attention or remedy.

that the Real Estate Assessment Center conduct a reinspection of Morris Park. After the reinspection is completed, Morris Park will be allowed to make distributions to the owner only if it has

- Received a passing score of 60 or above,
- Surplus cash, and
- Complied with the regulatory agreement.

### **Accounting Records Were Not Reconciled Monthly**

Morris Park officials did not reconcile their accounting records monthly. They stated that accounting records were reconciled before the independent public accountants prepared the annual audited financial statements and thought that would suffice. This condition occurred because there was a lack of documented accounting procedures and nursing home officials had not emphasized ensuring compliance with HUD requirements. HUD Handbook 4370.2, REV-1, paragraph 2-3(A), and the nursing home regulatory agreement, section 14, require that books, records, and contracts be maintained in reasonable condition at all times for proper audit and examination. In addition, HUD Handbook 4370.2, REV-1, paragraph 2-12(B)(5), requires that a monthly reconciliation be performed to ensure that all checks disbursed are accounted for. As a result of the deficiency noted above, HUD had no assurance that accounting records were reconciled monthly and errors or irregularities in the financial information were detected in a timely manner.

### **Audited Financial Statements Were Not Submitted in a Timely Manner**

Morris Park officials did not submit 2013 and 2014 audited financial statements in a timely manner. The 2013 and 2014 audited financial statements were due to HUD on April 1, 2014, and April 1, 2015, respectively.<sup>3</sup> However, officials submitted the 2013 audited financial statements on May 22, 2014, which was 51 days past the allowable due date. The 2014 audited financial statements had not been submitted as of June 2015. According to the nursing home regulatory agreement, section 18, the nursing home must submit to the commissioner audited financial statements in compliance with generally accepted auditing standards and government auditing standards within 90 days of the close of the project's fiscal year, which ends December 31. The condition described above occurred because officials did not ensure that audited financial statements were completed and submitted in a timely manner as required by the regulatory agreement. Further, officials stated that annually retained independent public accountants did not begin work to complete their financial statements until the second quarter of the fiscal year, or between April and June. Therefore, officials did not prioritize ensuring that financial statements were prepared on time. As a result, HUD officials could not effectively monitor or determine the financial condition of the nursing home.

### **Conclusion**

Morris Park officials generally managed funds in accordance with the regulatory agreement and HUD requirements. However, in 2013 and 2014, they made two \$60,000 distributions to the nursing home's owner, 1235 Pelham Parkway Realty, LLC, in violation of the regulatory

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<sup>3</sup> Since the fiscal year ends on December 31, regulations allow the financial statements to be audited and submitted up to 90 days after the fiscal year ends, no later than April 1.

agreement. In addition, officials did not perform monthly reconciliations of accounting records and submit audited financial statements in a timely manner. These conditions occurred because nursing home officials were not aware of all necessary requirements, compliance with HUD requirements was not emphasized, and accounting procedures were not documented. As a result, nursing home officials could not ensure that the distributions complied with the regulatory agreement, accounting records were reconciled monthly, and audited financial statements were provided in a timely manner.

### **Recommendations**

We recommend that the Director of HUD's Office of Residential Care Facilities instruct Morris Park officials to

- 1A. Establish and implement procedures to ensure that distributions are made to the owner only if the project complies with all requirements in the regulatory agreement, to include compliance with notices of physical inspection deficiencies.
- 1B. Establish and implement written accounting procedures to ensure that books and records are maintained in accordance with HUD requirements.
- 1C. Ensure that accounting records are reconciled monthly.
- 1D. Implement procedures to ensure that audited financial statements are prepared and submitted to HUD in a timely manner in accordance with the regulatory agreement.

# Scope and Methodology

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The review generally covered the period January 1, 2013, through December 31, 2014. We performed audit fieldwork from April 28 through June 30, 2015, at Morris Park located at 1235 Pelham Parkway North, Bronx, NY.

To accomplish our audit objective, we

- Reviewed HUD handbooks and the nursing home's policies and procedures.
- Obtained an understanding of the nursing home's financial controls.
- Interviewed officials of HUD's Departmental Enforcement Center and Morris Park.
- Reviewed the lessee's regulatory agreement between HUD and Morris Park and the owner's regulatory agreement between HUD and 1235 Pelham Parkway Realty, LLC.
- Reviewed the mortgage note between HUD and 1235 Pelham Parkway Realty, LLC.
- Reviewed bank statements and general ledgers for 2013 and 2014.
- Evaluated Morris Park's internal controls to identify potential weaknesses related to our objective.
- Reviewed data in HUD's Integrated Real Estate Management System.<sup>4</sup>
- Reviewed the 1235 Pelham Parkway Realty, LLC, audited financial statements for the fiscal years ending in 2013 and 2014.
- Reviewed Morris Park's audited financial statements for the fiscal year ending in 2013.

We performed a 100 percent review of the monthly mortgage payments, deposits and withdrawals to and from the reserve for replacement account, distributions to the owner, and repayments from the owner for the audit period, January 1, 2013, through December 31, 2014. We also performed limited testing of the general ledger accounts and accounts receivable for the period reviewed. In addition, we performed audit procedures to identify identity-of-interest transactions, including a review of Internal Revenue Service Form 1099 information for independent contractors. We also verified whether health and safety violations noted by HUD inspectors had been corrected by testing patient call buttons for 6 of 18 beds that were listed with violations of patient call buttons.

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<sup>4</sup> HUD's Integrated Real Estate Management System is the official source of data on the Office of Multifamily Housing Programs' portfolio of insured and assisted properties. It provides automated support to collect and maintain accurate data and enables program centers and hubs and Enforcement Center staff to perform servicing functions and implement enforcement actions as needed. This system is available on the Internet only to contract administrators.

While we used the data obtained from HUD's Integrated Real Estate Management System for informational purposes, our assessment of the reliability of the data in the system was limited to the data reviewed; therefore, we did not assess the reliability of this system.

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

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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:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.
- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

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.

We evaluated internal controls related to the audit objective in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance regarding the effectiveness of the internal control structure as a whole.

Accordingly, we do not express an opinion on the effectiveness of Morris Park's internal controls.