



U. S. Department of Housing and Urban Development
Office of Inspector General
New York/New Jersey Office
26 Federal Plaza – Room 3430
New York, NY 10278-0068

MEMORANDUM NO. 2010-NY-1804

June 4, 2010

MEMORANDUM FOR: Joan Spilman, Director, Office of Public Housing, Buffalo Field Office, 2CPH

//signed//

FROM: Edgar Moore, Regional Inspector General for Audit, New York/New Jersey, 2AGA

SUBJECT: The Rochester Housing Authority, Rochester, NY, Had Financial Control Weaknesses That Could Affect Its Capacity to Administer Recovery Act Funds

INTRODUCTION

We conducted a review of the Rochester Housing Authority's (Authority) administration of its capital funding program. We selected this Authority based upon indicators identified in a risk assessment of housing authorities that were allocated capital funds under the American Recovery and Reinvestment Act of 2009 (Recovery Act). The primary objective of our review was to evaluate the Authority's capacity in the areas of internal controls, eligibility, financial controls, procurement, and output/outcomes in administering its Recovery Act funds. The Authority had weaknesses in its financial controls that if left unaddressed could lead to its having a diminished capacity to effectively administer its \$5.9 million in supplemental capital funds received under the Recovery Act. Except for these issues, Authority officials demonstrated a positive attitude toward establishing and implementing additional financial controls, their procurement controls comply with regulations and their capital program outputs are in accordance with their established plans. Thus, overall, the Authority had the capacity to effectively administer its capital fund program supplemental funds provided under the Recovery Act according to applicable requirements.

For each recommendation without a management decision, please respond and provide status reports in accordance with U.S. Department of Housing and Urban Development (HUD) Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the review.

METHODOLOGY AND SCOPE

To gain an understanding of the Authority's administration of the capital fund program, we reviewed applicable laws, regulations, and HUD program requirements. In addition, we reviewed the Authority's procurement policy, conducted interviews with Authority personnel to gain an understanding of the internal controls, and tested the system of controls to determine whether the controls were functioning as intended. Also, we analyzed contract files and disbursement records for the review period October 2008 through September 2009. The review period was extended as necessary.

For the grant years 2005 through 2008, the Authority received more than \$18.5 million in capital funds to carry out capital and management activities. Effective March 18, 2009, the Authority received \$5.9 million in supplemental capital funds under the Recovery Act. The Authority obligated all of its Recovery funds by the prescribed March 17, 2010 deadline.

We performed our on-site work from September 2009 through February 2010 at the Authority's office located in Rochester, NY. Our work was not conducted in accordance with generally accepted government auditing standards. Under the Recovery Act, inspectors general are expected to be proactive and focus on prevention; thus, this report is significantly reduced in scope.

BACKGROUND

On February 17, 2009, the President signed the Recovery Act. This legislation includes a \$4 billion appropriation of capital funds to carry out capital and management activities for public housing agencies as authorized under Section 9 of the United States Housing Act of 1937, as amended. The Recovery Act requires that \$3 billion of these funds be distributed as formula funds and the remaining \$1 billion be distributed through a competitive process.

The Office of Management and Budget provided guidance establishing requirements for various aspects of Recovery Act planning and implementation. These requirements are intended to meet crucial accountability objectives. Specifically,

- Funds are to be awarded and distributed in a prompt, fair, and reasonable manner;
- The recipients and uses of all funds are to be transparent to the public, and the public benefits of these funds are to be reported clearly, accurately, and in a timely manner;
- Funds shall be used for authorized purposes, and instances of fraud, waste, error, and abuse are to be mitigated;
- Projects funded under the Recovery Act should avoid unnecessary delays and cost overruns;
- Program goals are to be achieved, including specific program outcomes and improved results on broader economic indicators.

RESULTS OF REVIEW

The Authority had weakness in its financial controls that if left unaddressed, could lead to its having a diminished capacity to effectively administer its capital fund program funds. Specifically, the Authority's program procedures and tracking system allowed for (1) ineligible expenses to be charged to the capital fund program, (2) capital funds to be disbursed for unsupported expenses, (3) eligible costs to not be reimbursed from capital fund program funds, and (4) inaccurate allocation of employee payroll expenses. Except for these issues, Authority officials demonstrated a positive attitude toward establishing and implementing additional financial controls, their procurement controls comply with regulations and their capital program outputs are in accordance with their established plans. Thus, overall, the Authority had the capacity in the areas of internal controls, eligibility, procurement, and output/outcomes to effectively administer its capital fund program.

1. Ineligible Expenses Charged to the Capital Fund Program

The Authority's procedures allowed for \$344,460 in fiscal year 2009 payroll expenses to be charged to the fiscal year 2008 capital fund program when there were no available funds. The Authority incurred more than \$409,000 in expenses that were charged to the capital fund program between March and September 2009. However, because the Authority had expended its budgeted administrative dollars from its awarded grants, these expenses had not been vouchered. Nevertheless, the Authority recorded the above payroll expenses as being available to its 2008 capital fund program when funds were not available. The Authority's procedures would have allowed it to transfer the expenses to the 2009 capital fund program and withdraw 2009 capital funds when they became available. However, the Authority's 2009 capital fund program grant was not awarded until September 2009; the annual contributions contract amendment provided an effective date of September 15, 2009. Regulations at 24 CFR (Code of Federal Regulations) 905.120 provide that a public housing agency shall obligate any assistance received not later than 24 months after the date on which the funds become available. Therefore, since there were no more 2008 capital funds available and these expenses were incurred before the 2009 capital funds were made available, the \$344,460 in payroll expenses is considered ineligible and should not be charged to the capital fund program.

In addition, Authority officials made \$35,493 in ineligible withdrawals of capital program funds. Specifically, the Authority withdrew \$11,931 in capital funds from the fiscal year 2008 grant due to a clerical mistake. Authority officials carried forward the total from the operations budget line item on the capital fund program expense detail sheet to the fees and costs budget line item, thus having no expenditures to support \$11,931 in withdrawals for fees and costs. Also, the Authority withdrew \$22,544 in capital funds, representing expenses from fiscal year 2007 and 2008 grants, using the same expenses that were used to support previous voucher requests. For example, the Authority used the same administrative expenses for two voucher requests as a result of not properly accounting for an accrual before making the second voucher request. Further, the Authority withdrew \$1,018 in administrative expenses from fiscal year 2006 and 2008 grants, consisting of items that were not actual employee benefits and thus were not eligible expenses under the capital fund program. Regulations at 24 CFR 85.20 provide that fiscal control and accounting procedures be sufficient to permit the tracing of funds to a level of expenditures

adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes. Accordingly, we consider the use of \$35,493 in capital funds to be ineligible.

Lastly, Authority officials reclassified \$2,811 in capital fund program expenses related to relocation costs based on our inquiries regarding its eligibility. There was a series of purchase orders for relocated tenants' cable television service that were charged to the Authority's capital fund program dwelling structure budget line item. However, the Authority had not budgeted for relocation expenses and did not explain how they were eligible for funding under the capital fund program. Due to the lack of documentation, Authority officials decided to reallocate the \$2,811 cost to its operating account, resulting in a realized cost savings to the capital fund program. HUD Handbook 7585.3G provides eligible costs that can be incurred during relocation.

2. Capital Program Funds Disbursed for Unsupported Expenses

The Authority vouchered \$169,542 in capital fund program funds for multiple expenses paid from the fiscal year 2005 and 2006 grants without the proper supporting documentation. The majority of the withdrawals were for expenses that occurred months or years before the voucher request. The Authority's financial control system provided no assurance that these expenses had not been requested in prior capital fund program vouchers. In addition, the Authority was unable to provide adequate supporting documentation for \$7,747 in payroll expenses paid from the fiscal year 2006 grant. Consequently, we consider the use of \$177,289 in capital funds to be unsupported pending a HUD eligibility determination. Regulations at 24 CFR 85.20 provide that fiscal control and accounting procedures be sufficient to permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.

3. Eligible Costs Not Reimbursed From Capital Program Funds

The Authority failed to voucher \$3,264 in eligible modernization-related expenses from its capital fund program. The Authority pays its vendors from its operating account and then requests reimbursement from capital funds. However, a comparison of its tracking system to the capital fund program vouchers indicated that these expenses had not been included in any capital program funds requests. Thus, these expenses should be requested from capital funds and reimbursed to the operating account. By reimbursing the operating account, these funds will be put to better use.

4. Inaccurate Allocation of Employee Payroll Expenses

The Authority incorrectly charged 100 percent of the payroll expenses pertaining to the director of property development to the capital fund program. In addition to the director's duties pertaining to the capital fund program, we were informed that the director was instrumental in the conversion of low-rent housing units to Section 8. Regulations at 24 CFR 968.112(j) provide that eligible administrative costs are those necessary for the planning, design, implementation, and monitoring of physical and management improvements. The Authority acknowledged that the director's time should have been allocated over a number of programs. For fiscal year 2009,

Authority officials explained that they plan to reallocate a percentage of the director's time to activities funded under the supplemental Recovery Act, the capital fund program, Section 8 conversion, and other development activities. Starting with fiscal year 2010, the director would be charging 50 percent of his time to activities funded under the supplemental Recovery Act and 50 percent to Section 8 conversion and other development activities. Accordingly, we recommend that HUD officials review and monitor the Authority's allocation plan to ensure that costs for payroll expenses are properly charged to the supplemental Recovery Act capital fund program and the regular capital fund program.

CONCLUSION

The Authority needs to correct financial control weaknesses identified to ensure HUD that the Recovery Act funds will be disbursed in accordance with regulations. These financial control weaknesses related to charging ineligible and unsupported costs to the capital fund program, not reimbursing eligible expenses from the capital fund program, and the improper allocation of employee payroll expenses. We attribute these weaknesses to the Authority's (1) failure to follow established procedures for charging eligible and supported expenses to the capital fund program, (2) lack of a quality control system to ensure that expenses were properly disbursed, (3) inadequate tracking system to ensure that eligible capital fund program expenses were vouchered in a timely manner, and (4) lack of an accurate allocation plan. Except for these issues, Authority officials demonstrated a positive attitude toward establishing and implementing additional financial controls, their procurement controls comply with regulations and their capital program outputs are in accordance with their established plans. Thus, overall, the Authority had the capacity to administer capital funds provided under the Recovery Act.

RECOMMENDATIONS

We recommend that the Director of HUD's Buffalo Office of Public Housing

- 1A. Monitor and oversee the Authority's charges and withdrawals for capital fund program administrative expenses and ensure that only allocable 2009 payroll expenditures are charged to the Authority's capital fund programs. This measure will assure HUD that capital funds, including those provided under the Recovery Act, will be disbursed in accordance with regulations.

We also recommend that the Director of HUD's Buffalo Office of Public Housing, instruct the Authority to

- 1B. Ensure that \$379,953 in ineligible charges and withdrawals of capital funds (\$344,460 in ineligible payroll expenses, \$11,931 for a clerical mistake, \$22,544 in duplicate costs, and \$1,018 in non-capital fund program administrative expenses) are properly accounted for and reimbursed to HUD from non-Federal funds.

- 1C. Provide documentation to justify the \$177,289 in unsupported withdrawals (\$169,542) and payroll expenses (\$7,747) so that HUD can make an eligibility determination. Any unsupported costs determined to be ineligible should be reimbursed to HUD from non-Federal funds.
- 1D. Provide documentation to HUD to ensure that \$2,811 in relocation expenses was reclassified and charged to the Authority's operating fund and that \$3,264 in eligible modernization-related expenses is reimbursed from capital funds, thereby ensuring that \$6,075 is put to better use.
- 1E. Establish procedures that will ensure that allocation plans are reviewed annually and updated to ensure that allocation percentages are accurate.
- 1F. Establish and implement quality control policies and procedures that require periodic examinations and independent reconciliations of capital fund program voucher requests to ensure that vouchers are supported, eligible, and in accordance with capital fund program policies and procedures.
- 1G. Review its financial controls for tracking capital fund expenditures and revise the existing financial controls to ensure that capital fund program expenses are requested in a timely manner to better match the expenses incurred in one year with the funding for that year, and that all eligible expenses are included in voucher requests.

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1B	\$379,953		
1C		\$177,289	
1D			<u>\$6,075</u>
Total	<u>\$379,953</u>	<u>\$177,289</u>	<u>\$6,075</u>

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.

2/ 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.

3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. If the Authority implements our recommendation to provide documentation to HUD to ensure that relocation expenses were reclassified and charged to its operating fund and that eligible modernization-related expenses are reimbursed from capital funds, it will ensure that \$6,075 in funds is put to better use.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Anthony P. DiBiase

Executive Director / CEO
Rochester Housing Authority
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May 4, 2010

Ms. Karen A. Campbell
U.S. Department of Housing and Urban Development
Office of Inspector General
26 Federal Plaza - Room 3430
New York, NY 10278

Dear Ms. Campbell:

The Rochester Housing Authority, hereafter also referred to as 'the Authority', was pleased with the Inspector General's finding that 'the Authority had the capacity to effectively administer its capital fund program supplemental funds provided under the Recovery Act according to applicable requirements'. The Rochester Housing Authority wishes to acknowledge the professionalism and thoroughness of the Office of the Inspector General's staff in conducting their audit. The Authority welcomes such audits and uses their findings as a means to continually upgrade and tighten its controls and procedures. **COMMENT 1**

Given the Audit report is a matter of public domain, the Authority feels it is important to submit the following comments regarding the specific findings and wording within the document:

Introduction — Page 1

The Office of the Inspector General states that 'We selected this Authority based upon indicators identified in a risk assessment of housing authorities that were allocated capital funds under the American Recovery and Reinvestment Act of 2009'. The Rochester Housing Authority would like to point out that it has always received the rating of "standard performer" by the U.S. Department of Housing and Urban Development (HUD) narrowly missing "high performer" status and would object to the conclusion drawn from this statement that funds entrusted to the Authority are at a higher risk than those entrusted to other comparable authorities. **COMMENT 2**

Methodology and Scope — Page 2

As a basis for judging the materiality of the numbers found in the audit report, Rochester Housing Authority would like to mention that during the 12 month period reviewed (October 2008 through September 2009), the Authority requisitioned \$7,457,102 in capital funds. **COMMENT 3**

Section 1 - Ineligible le Expenses Charged to the Capital Fund Program — Page 3

Rochester Housing Authority would like to emphasize the fact that at the time of the audit, reimbursement of the expenses in question were not drawn down from HUD LOCCs and resided in a separate account on its Central Office Cost Center (COCC) balance sheet pending disposition. **COMMENT 4**

The Authority has subsequently charged the expenses in question to its COCC (non-Federal funds) as part of its Fiscal 2009 year end closing entries. The Authority believes the amount of the payroll expenses in question was \$340,768 versus the \$344,460 stated. **COMMENT 5**

In the second paragraph, two charges representing \$18,687 of the \$22,544 were caught and corrected through the Authority's own routine audit of its projects prior to the Inspector General's audit. **COMMENT 6**

Later in the same paragraph, the \$1,018 in administrative charges referred to were found to be legitimate expenses chargeable to the capital program but were misidentified and charged to the incorrect (Administrative) line item within the program. **COMMENT 7**

Section 2 — Capital Funds Disbursed for Unsupported Expenses — Page 4

The Rochester Housing Authority acknowledges the expenses in question were not processed in a timely manner, however the Authority believes it had provided the auditors with sufficient backup to support the charges. The Authority possesses, and forwarded copies of all the invoices which account for the \$169,542 and maintains a contract register listing all invoices charged to each of its CFP grants. Routine Internal review of the registers eliminated the possibility that these expenses had been previously charged to the applicable project. **COMMENT 8**

Regarding the \$7,747 in payroll expenses, the Authority's routine internal review of its programs determined that according to its payroll system reports, the capital grant in question was allocated a given dollar amount of wages and after examining the project register, it was found the amount of wages actually booked to the project was \$7,747 less than the payroll system figure, at which point a correcting entry was made. **COMMENT 9**

Section 4 — Improper Allocation of Emplo^yee Payroll Expenses — Page 4

Rochester housing Authority would like to take exception to the wording found in the title of this section and make a clarification regarding this section's content.

In the title of the section itself, the use of the word 'Improper' may allege 'impropriety' which may be interpreted by the reader to connote an intentional attempt to deceive. 'Inaccurate' or a word of similar meaning would be preferred. **COMMENT 10**

After analyzing the time spent by the Director of Property Development, the decision has been made to allocate 70 percent of his time to activities funded under the supplemental Recovery Act and 30 percent to Section 8 conversion and other development activities which are costs absorbed by the Authority's Central Office Cost Center. The audit stated that position's time would be split 50/50. **COMMENT 11**

Conclusion

Regarding point number 2, 'the lack of a quality control system', the Rochester Housing Authority would like to restate that several of the items detected during the audit were discovered and corrected via the Authority's own internal auditing of its programs. This was completed prior to the Inspector General's audit. **COMMENT 12**

The wording of point number 4 'lack of an established allocation plan' implies the Authority has no allocation plan for allocating its common charges. The Authority would like to note that as part of its annual budgeting process, the Authority updates and uses an allocation plan (Salary allocations by individual based on job duties, applicable Public Housing charges allocated based on units, Information Technology charges based on the number of personal computers at its various locations, etc). The Authority does acknowledge the need to continuously review the salary allocations as duties and responsibilities change. **COMMENT 13**

In conclusion, the Rochester Housing Authority would again like to thank the Office of the Inspector General for its due-diligence. The Authority is confident it will successfully resolve issues identified herein during the follow up with HUD's Buffalo Office of Public Housing as recommended at the end of the report.

Respectfully submitted,

//signed//

Mark D. Hill

Accounting Supervisor

Rochester Housing Authority

//signed//

Anthony P. DiBiase

Executive Director

Rochester Housing Authority

OIG Evaluation of Auditee Comments

- Comment 1** Officials for the Authority state that they are pleased with the Inspector General’s finding that “the Authority had the capacity to effectively administer its capital fund program supplemental funds provided under the Recovery Act according to applicable requirements”. However, although overall, the Authority had the capacity to effectively administer its capital fund program supplemental funds provided under the Recovery Act, the Authority had weaknesses in its financial controls that if left unaddressed could lead to its having a diminished capacity to effectively administer its \$5.9 million in supplemental capital funds.
- Comment 2** Officials for the Authority state that the Authority has always received a rating of “standard performer” by HUD narrowly missing “high performer” status and Authority officials would object to the conclusion drawn from this statement that funds entrusted to the Authority are at a higher risk than those entrusted to other comparable authorities. Our organization identified public housing capital funding as a high-risk funding category under the Recovery Act. As such, regardless of the Authority’s HUD designated performance level, our review was initiated based on a risk assessment of authorities receiving Recovery Act funds. The Authority received the second highest amount of Recovery Act funds in relation to the authorities administered by the HUD Buffalo Office. Further, the Authority, which was allocated \$5.9 million in capital funds under the Recovery Act, owns and manages 31 housing developments with 2,495 total units, which makes it large enough to be high risk.
- Comment 3** Officials for the Authority indicate that for judging materiality of the numbers found in the audit report, the Authority requisitioned \$7,457,102 in capital funds during the review period. To clarify the scope of our review, we adjusted the report to reflect the amount of funding the Authority received in the scope section of the report instead of as originally detailed in the background section. Nevertheless, the deficiencies reported pertain to our concerns with the Authority’s controls over disbursing capital program funds.
- Comment 4** Officials for the Authority contend that reimbursement of the ineligible expenses charged to the capital fund program were not drawn down from HUD LOCCS and resided in a separate account on its Central Office Cost Center balance sheet pending disposition. However, we determined that due to the Authority’s financial control weaknesses, its system allowed for 2009 payroll expenses to be charged to the 2008 capital fund program when no such funds were available. Had this not been brought to the attention of officials for the Authority, the Authority’s procedures would have allowed it to transfer the expenses to the 2009 capital fund program and withdraw 2009 capital funds when they became available. However, the Authority’s 2009 capital fund program grant was not awarded until September 2009, as the annual contributions contract amendment provided an effective date of September 15, 2009.

- Comment 5** While officials for the Authority agree that the ineligible 2009 payroll expenses should not have been charged to the capital fund program, and they subsequently charged the expenses to its COCC (non-Federal funds), they believe that the correct amount should be \$340,768 versus the \$344,460 stated. The \$344,460 represents our calculation of ineligible payroll expenses charged to the capital fund program between March and September 2009. The difference between the two calculations should be reconciled between HUD and Authority officials during the audit resolution process.
- Comment 6** Officials for the Authority state that two charges representing \$18,687 of the \$22,544 were caught and corrected through the Authority's own routine audit of its projects prior to the Inspector General's audit. The OIG acknowledges that the Authority made some efforts to correct past errors. However, we are still concerned with the financial control weaknesses that allowed the errors to occur.
- Comment 7** Officials for the Authority stated that the \$1,108 turned out to be an eligible capital fund expense. Nevertheless, we both agree that the \$1,018 in administrative expenses were charged to the incorrect line item within the program, and that needs to be adjusted.
- Comment 8** Officials for the Authority acknowledge that the unsupported expenses were not processed in a timely manner. The officials believe that they provided the auditors with sufficient backup to support the charges. However, as discussed during the exit conference, the Authority needs to provide evidence that in fact none of these unsupported expenses have been vouchered in the past. This support will need to be provided to HUD officials during the audit resolution process for their eligibility determination.
- Comment 9** Officials for the Authority state that the Authority's routine internal review identified the \$7,747 discrepancy in payroll expenses booked and that a journal entry was made to correct the error. However, at the time we reviewed the payroll expenses, there was inadequate documentation to support \$7,747 in payroll expenses. HUD officials will need to review this documentation during the audit resolution process to determine if the support is adequate.
- Comment 10** Officials for the Authority contend that the use of the word "Improper" pertaining to the allocation of employee payroll expenses may allege "impropriety". As such, we have changed the word improper to inaccurate and we have included an additional recommendation to ensure that allocation plans are accurate and should be updated annually.
- Comment 11** Officials for the Authority concur that they incorrectly charged 100 percent of the director of property development's payroll expenses to the capital fund program. As a result, the Authority will be allocating 70 percent of his time to activities funded under the Recovery Act and 30 percent of his time to Section 8 conversion

and other development activities absorbed by the COCC in the future, not the 50/50 as stated in the report.

Comment 12 Officials for the Authority state that several of the items detected during the audit were discovered and corrected via the Authority's own internal auditing of its programs, which is true. However, the deficiencies that were subsequently corrected should be provided to HUD officials during the audit resolution process for an eligibility determination.

Comment 13 Officials for the Authority contend that the "lack of an established allocation plan" implies the Authority has no allocation plan for allocating its common charges. While the Authority does have an allocation plan, officials for the Authority concur that the salary allocations need to be continuously reviewed as duties and responsibilities change. Accordingly, we have changed the wording of item 4 in our conclusion to state that we attribute the weakness to the lack of an accurate allocation plan, and as stated earlier we added a recommendation that the allocation plan should be updated annually.