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TO: Shawn Sweet, Acting Director of Public Housing Hub, 5DPH
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FROM: 
Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: The Housing Authority of the City of Terre Haute, IN, Substantially
Mismanaged Its Capital Fund Program and Lacked Capacity To Adequately
Administer Its Recovery Act Funds

HIGHLIGHTS

What We Audited and Why

We audited the Housing Authority of the City of Terre Haute, IN's (Authority) Public Housing Capital Fund program (program). We selected the Authority based on our audits of its nonprofit development activities (see Office of Inspector General (OIG) audit report #2009-CH-1011, issued July 2009) and as part of OIG's initiative to evaluate public housing authorities' capacity to administer the capital funds provided under the American Recovery and Reinvestment Act of 2009 (Recovery Act). Our audit objectives were to determine whether the Authority (1) properly administered its program and (2) had the capacity to administer its Recovery Act funds.

What We Found

Under the direction of the former executive director, the Authority violated its annual contributions contract (contract) with the U.S. Department of Housing and Urban Development (HUD) when it obtained a \$2.3 million construction loan and a \$2 million line of credit to finance capital improvements without HUD

approval. Further, the Authority did not follow HUD's and its own procurement requirements and failed to pay its maintenance staff and a contractor the appropriate Federal labor standard wage rates as required by the Davis-Bacon Act.

The Authority obligated its Recovery Act funds in a timely manner. However, it lacked adequate written policies and procedures and staff knowledgeable of HUD's and other Federal procurement requirements. Therefore, it lacked sufficient capacity to expend the funds.

As a result, the Authority encumbered \$2.3 million of its project assets, and HUD lacked assurance that it (1) used more than \$1.4 million in program funds for their intended purposes, (2) operated its program in an efficient manner, and (3) had the capability to effectively expend its Recovery Act funding. Further, the Authority owed more than \$49,000 in wage restitution.

What We Recommend

We recommend that the Acting Director of HUD's Cleveland Office of Public Housing require the Authority to (1) provide documentation of HUD's approval of the construction loan, (2) reimburse HUD nearly \$800,000 for the interest incurred on the loan from 2000 to 2007 and reimburse its project more than \$70,000 for interest incurred on the loan after 2007 from non-Federal funds, (3) provide documentation showing that HUD approved the line of credit and the use of program funds for reimbursement of previously incurred expenses, (4) reimburse its program \$129,872 from non-Federal funds for the interest paid on the line of credit, (5) reimburse its current and/or former maintenance employees and contractor \$49,532 from non-Federal funds for wage restitution, and (6) implement adequate procedures and controls to address the findings cited in this audit report.

We also recommend that HUD's Acting Director

- Inform the Acting Deputy Assistant Secretary for Field Operations of the Authority's actions, which may result in a substantial default of its contract.
- Consult with HUD's Office of General Counsel to determine whether the construction loan encumbered and/or pledged the Authority's project assets. If the loan only encumbered the assets, a determination is needed to conclude whether the loan can be retroactively approved. If the loan cannot be approved, the Authority should be required to reimburse its program more than \$1.6 million and its project more than \$800,000 from non-Federal funds.
- Consult with HUD's Office of General Counsel to determine the appropriateness of the Authority's using its fiscal year 2008 program funds

to pay for the line of credit expenses that were previously incurred. If the use of the funds was not appropriate and should not be retroactively approved, the Authority should reimburse its program more than \$1.4 million from non-Federal funds for its fiscal year 2008 program award.

- Acquire capacity to manage its Recovery Act and other similar funding, including, but not limited to, staff persons knowledgeable in Federal procurement requirements or contracting for this expertise, developing specific procedures for financial reporting, management controls, and procurement.
- Incorporate the applicable recommendations cited in this audit report into the Authority's memorandum of agreement with HUD.

Further, we recommend that HUD's Acting Director, in conjunction with the Director of HUD's Departmental Enforcement Center, pursue the appropriate administrative sanction(s) against the Authority's former executive director for failing to enforce HUD's requirements.

We also recommend that HUD's Associate General Counsel for Program Enforcement determine legal sufficiency and if legally sufficient, pursue remedies under the Program Fraud and Civil Remedies Act against the Authority's former board chairperson/principals for incorrectly certifying that the information contained in the Authority's annual plans was true and accurate when it was not.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided our discussion draft audit report to the Authority's executive director, its board president, and HUD's staff during the audit. We held an exit conference with the Authority on June 1, 2010. We asked the Authority's executive director to provide comments to our discussion draft report by June 18, 2010. The executive director provided written comments, dated June 18, 2010, that generally disagreed with our findings and recommendations. The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Housing Authority of the City of Terre Haute, IN, (Authority) was established on April 28, 1960, as a municipal corporation under Section 36-7-18-4 of the Indiana Code to provide decent, safe, and sanitary housing to low-income families under the United States Housing Act of 1937. The Authority is governed by a seven-member board of commissioners appointed by the mayor of Terre Haute to 4-year terms. The board governs the business, policies, and transactions of the Authority. The executive director is appointed by the board and has overall responsibility for carrying out the board's policies and managing the Authority's day-to-day operations. The Authority's books and records are located at 2001 North 19th Street, Terre Haute, IN. The Authority owns 868 low-rent public housing units in six projects and has the authority to administer 917 Section 8 vouchers. As of January 31, 2010, of the 917 Section 8 vouchers, 858 were under lease. Further, the Authority manages 171 housing units for its nonprofit and for-profit entities.

For fiscal year 2007, the Authority received an overall public housing assessment score of 63 out of the maximum of 100. The U.S. Department of Housing and Urban Development (HUD) designated the Authority as substandard financially. Based on the Authority's assessment score, HUD was drafting a memorandum of agreement (agreement) with the Authority to address its deficiencies. As of July 19, 2010, the agreement had not been executed.

The Public Housing Capital Fund program (program) is administered by HUD's Office of Public and Indian Housing. Capital funds are for the development, financing, and modernization of public housing developments and for management improvements. The Quality Housing and Responsibility Act of 1998 converted HUD's Comprehensive Grant and Comprehensive Housing Assistance programs to the Public Housing Capital Fund program.

The program provides annual funding to public housing agencies for the development, financing, and modernization of public housing developments and for management improvements. The program must directly support public housing rental projects or their residents. Eligible activities generally include redesign, reconstruction, and accessibility improvements for public housing units; vacancy reduction; deferred maintenance needs; the replacement of obsolete utility systems and dwelling equipment; planned code compliance; demolition and replacement of units; homeownership activities; management improvements; and transfers to operations.

A public housing agency is required to obligate its program assistance within 24 months from the date the funds are available to the agency for modernization or development activities, or the date the agency accumulates adequate funds to undertake modernization, rehabilitation, or new construction of units. Capital funds must be expended within 48 months from the date they are made available. On September 17, 2009, the Authority was awarded \$1,348,962 in capital funding.

On February 17, 2009, the President signed the American Recovery and Reinvestment Act of 2009 (Recovery Act) into law. The Recovery Act provided \$4 billion to public housing agencies to carry out capital and management activities, including modernization and development of

public housing. Under the Recovery Act, public housing agencies are required to obligate 100 percent of the funds within 1 year of the date on which funds become available to the agency for obligation and expense 60 percent within 2 years and 100 percent within 3 years of such date. Public housing agencies report their obligations and expenditures using HUD's Line of Credit Control System (system). HUD was required to recapture remaining program funds of public housing agencies that failed to meet the obligation deadline of March 17, 2010, and expenditure deadlines. On March 17, 2009, the Authority was awarded \$1,794,175 in Recovery Act funds

Our audit objectives were to determine whether the Authority (1) properly administered its program and (2) had the capacity to administer its Recovery Act funds.

RESULTS OF AUDIT

Finding 1: The Authority Obtained a \$2.3 Million Construction Loan by Encumbering Project Assets Contrary to Its Contract With HUD

The Authority encumbered project assets when it obtained a \$2.3 million construction loan to finance electrical system upgrades to support the installation of air conditioning units at its senior housing development, Dreiser Square. The loan agreement authorized Transamerica Public Finance (Transamerica) to obtain a security interest in the Authority's assets. Further, the Authority incurred interest expenses totaling more than \$800,000 on the construction loan and did not obtain an energy audit before the upgrades. The problem occurred because the Authority's former board failed to provide adequate oversight of the Authority's operations. As a result, the Authority violated its contract with HUD and subjected itself to unnecessary risks had it defaulted on the loan. Also, HUD and the Authority lacked assurance that the electrical upgrades were cost effective. Further, the Authority's failure to fully disclose its non-Federal financing resulted in its submitting incorrect statements to HUD.

The Authority Violated Its Contract

On December 22, 1999, the Authority's former board approved resolution number 99-15, authorizing the bid of more than \$2,284,011 from its utility provider, Cynergy Business Solutions, to perform electrical system upgrades and install 256 air conditioning units at its senior housing development, Dreiser Square.

Therefore, the Authority's former executive director obtained a construction loan with Transamerica, which included a master lease purchase agreement (purchase agreement). The upgrades included the installation of wires in the walls of the housing units to allow for the installation of electrical outlets and a light in the attic for each air conditioning unit. Further, the purchase agreement included the installation of new underground transformers, individual unit utility meters, panels, and other electrical improvements.

The terms and conditions of the purchase agreement included a provision that allowed Transamerica to have a security interest, which represented a lien on the equipment and all attachments such as wiring. According to the Authority's contract, the Authority shall not in any way encumber any project without the approval of HUD. However, Transamerica filed a financing statement with the State of Indiana on July 14, 2004. The statement listed it as the secured party and the Authority as the debtor. The Authority did not disclose the loan in its annual plans to HUD and was unable to provide documentation indicating that HUD approved the loan, contrary to its contract with HUD (see appendix C).

The Authority Used Program Funds To Repay the Loan

The Authority used program funds to pay the principal and interest on the construction loan. According to the loan's amortization schedule, the Authority agreed to semiannual payments of principal and interest over a 10-year period. Therefore, from July 2000 until July 2007, the Authority made 15 semiannual payments totaling \$2,408,623. This amount included \$791,650 in interest. According to Office of Management and Budget Circular A-87, attachment B, section 23(a), costs incurred for interest on borrowed capital or the use of a governmental unit's own funds is unallowable.

In October 2008, the Authority, under the direction of the new executive director, discontinued using program funds to repay the loan. Therefore, based on the advice from its fee accountant, Hawkins, Ash, Baptie & Company, Limited Liability Partnership, the Authority charged the remaining five payments, totaling \$802,874, to Dreiser Square since the Authority had transitioned to asset management. This amount included \$70,106 in interest.

The Authority Submitted Inaccurate Certifications to HUD

The Authority submitted annual plans to HUD that contained inaccurate information. It disclosed in its 2000 annual plan that it would use capital funds to update the electrical system at Dreiser Square. However, it used the funds to pay the principal and interest on the \$2.3 million construction loan, as previously mentioned. Further, the Authority did not disclose the loan on its statement of financial resources. According to HUD's regulations at 24 CFR (Code of Federal Regulations) 903.7(c), the statement must address the financial resources that are available to the public housing agency for the support of Federal public housing and tenant-based assistance programs administered by the public housing agency during the plan year. The statement also should include the non-Federal sources of funds supporting each Federal program and state the planned uses for the resources.

In its 2001 through 2007 annual plans, the Authority reported yearly electrical upgrade costs. However, it did not disclose that these costs were incurred for work that was performed and completed in 2000 as part of the debt service costs for the construction loan that was executed in 1999.

Further, the Authority's 2005 through 2007 annual plans required it to specifically indicate whether it intended to use program funds to repay debt incurred to finance capital improvements. The Authority was also required to disclose the

development(s) in which such improvements would be made, show how the proceeds of the financing would be used, and state the amount of the annual payments that would be required to service the debt. However, the Authority consistently indicated that it did not propose to use any portion of its program funds to repay debt incurred to finance capital improvements. Therefore, it did not provide the necessary disclosures. Additionally, since 2005 as part of its annual plan submission, the Authority submitted forms HUD-50076 or HUD-50077, certifying that all of the information contained in its annual plan was true and accurate. The Authority's former board chairperson signed the forms.

The Program Fraud Civil Remedies Act of 1986 (231 U.S.C. (United States Code) 3801) provides Federal agencies, which are the victims of false, fictitious, and fraudulent claims and statements, with an administrative remedy (1) to recompense such agencies for losses resulting from such claims and statements; (2) to permit administrative proceedings to be brought against persons who make, present, or submit such claims and statements; and (3) to deter the making, presenting, and submitting of such claims and statements in the future.

The Authority Did Not Perform an Energy Audit Before Obtaining the Loan

The Authority did not have an energy audit to determine the payback period for its energy conservation measures before obtaining the construction loan. Further, it did not perform a cost benefit analysis when changing to individual unit utility meters. According to HUD regulations at 24 CFR 965.302, all public housing agencies shall complete an energy audit for each public housing agency-owned project under management not less than once every 5 years. Energy audits shall analyze all of the energy conservation measures and the payback period for these measures. Further, HUD's regulations at 24 CFR 965.402 states that a cost benefit analysis shall be made to determine whether a change to individual meters will be cost effective. In 2009, the Authority obtained an energy audit from Myszak & Palmer, Incorporated. The company was originally contracted in 2007 to perform an energy audit.

Conclusion

The Authority's former board failed to provide adequate oversight of the Authority's operations. According to the former board chairperson, the board was not aware that it could be involved in the administration of the Authority. Therefore, the former executive director administered the Authority's programs without the board's full involvement. As a result of the \$2.3 million construction loan and the Authority's noncompliance with Federal requirements regarding energy conservation, the Authority encumbered project assets, and HUD and the

Authority lacked assurance that the electrical upgrades were cost effective. Further, the Authority's failure to fully disclose its non-Federal financing resulted in its submitting inaccurate statements to HUD.

Recommendations

We recommend that the Acting Director of HUD's Cleveland Office of Public Housing require the Authority to

- 1A. Provide documentation to support HUD's approval of the construction loan cited in this finding.
- 1B. Reimburse HUD \$791,650 for the interest incurred on the loan from 2000 to 2007 and reimburse its project \$70,106 for the interest incurred on the loan after 2007 from non-Federal funds.

We also recommend that the Acting Director of HUD's Cleveland Office of Public Housing

- 1C. Inform the Acting Deputy Assistant Secretary for Field Operations of the Authority's actions that encumbered project assets without HUD approval.
- 1D. Consult with HUD's Office of General Counsel to determine whether the loan encumbered and/or pledged the Authority's project assets. If the loan only encumbered the assets, a determination is needed regarding whether the loan can be retroactively approved (see recommendation 1A). If the loan cannot be approved, the Authority should be required to reimburse its program \$1,616,973 and its project \$802,874 from non-Federal funds. The funds due to the project should be deposited into the project's restricted operating reserve.

We also recommend that the Acting Director, in conjunction with the Director of HUD's Departmental Enforcement Center,

- 1E. Pursue the appropriate administrative sanction(s) against the Authority's former executive director for failing to enforce HUD's requirements.

We also recommend that HUD's Associate General Counsel for Program Enforcement

- 1F. Determine legal sufficiency, and if legally sufficient, pursue remedies under the Program Fraud and Civil Remedies Act against the Authority's former board chairperson/principals for incorrectly certifying that the information contained in the Authority's annual plans was true and accurate when it was not.

Finding 2: The Authority Encumbered Project Assets When It Obtained a Bank Line of Credit To Finance Capital Improvements

The Authority encumbered project assets when it obtained a promissory note for a \$2 million revolving line of credit with First Financial Bank (bank) to finance its capital improvements. The note contained a setoff provision that allowed the bank to seize the Authority's accounts with the bank if it defaulted on the note. The Authority also obligated program funds before they were available to reimburse withdrawals from its line of credit. Further, it paid more than \$129,000 in interest on the line of credit. The problems occurred because the Authority lacked adequate procedures and controls to ensure that it complied with its contract and the former board did not provide oversight of the former executive director. As a result, HUD lacked assurance that the Authority used more than \$1.4 million in program funds for their intended purposes.

The Authority Obtained a Promissory Note To Finance Capital Improvement

On May 2, 2000, the Authority obtained a promissory note for a \$2 million revolving line of credit with the bank. The terms and conditions of the promissory note contained a setoff provision that allowed the bank to collect the amounts owed from all of the Authority's accounts with the bank if the Authority defaulted on the loan. The Authority used the bank to maintain its general fund account. According to the Authority's contract, the Authority shall not encumber any project assets without the approval of HUD (see appendix C).

The promissory note did not indicate a specific purpose for the line of credit; however, according to the bank's loan officer, the Authority obtained the line of credit to finance its working capital needs. Further, in reviewing the Authority's records, we determined that the Authority would reimburse withdrawals from its line of credit after receiving program funds. Although the Authority's general ledger failed to identify the source of funds when the Authority paid for capital fund improvements, its former finance director maintained a separate worksheet to account for the line of credit withdrawals and reimbursements.

The Authority received more than \$1.4 million in program funding for fiscal year 2008. However, it had already obligated the funds to reimburse withdrawals from its line of credit for capital improvement costs that were incurred in 2006 and 2007. The Authority's obligation of preawarded program funds to pay for costs that had already been incurred and paid using its line of credit was contrary to its program requirements and its contract with HUD. According to the Authority's program amendment to its contract, the date of the amendment was the date the funds became available for obligation.

The Authority Hired a Consulting Firm To Review Its Program

In 2008, after receiving a draft audit report from its prior independent public accountant questioning more than \$1.3 million in program expenditures in its fiscal year 2007 financial statements, the Authority hired two certified public accountants as consultants to review its program. In reviewing the consultants' report, we determined that the report disclosed the following information:

- For the period 2000 to 2008, the Authority had followed the practice of spending and charging expenditures to the program before the actual grant award and money were received from HUD. The Authority had in essence spent its program funds a full year in advance of receiving the funds.
- To help fund these expenditures, the Authority executed a bank line of credit for \$2 million annually. It did not receive approval from HUD for the bank line of credit and/or provide justification for spending funds on capital improvements in advance of annual grant awards.
- As of September 30, 2006, the Authority had spent \$1,690,071 earmarked for the 2007 program. These funds were not received until September 2007 and amounted to only \$1,303,033, or \$387,038 short of the actual expenditures. The \$387,038 shortfall was rolled over into program year 2008. Additionally, as of September 30, 2007, the Authority had already charged \$1,324,418 to the 2008 program.

In 2008, the Authority discontinued using the line of credit. However, it had already incurred and paid more than \$129,000 in interest.

Conclusion

The Authority lacked adequate procedures and controls to ensure that it complied with its contract, and the Authority's board did not provide oversight of the former executive director. As a result, HUD lacked assurance that the Authority used its fiscal year 2008 program award of \$1,417,421 for its intended purposes. Additionally, the Authority was unable to provide documentation to support that HUD approved its use of program funds to reimburse the line of credit.

Recommendations

We recommend that the Acting Director of HUD's Cleveland Office of Public Housing require the Authority to

- 2A. Provide documentation to support that HUD approved the line of credit and the use of program funds for reimbursement of previously incurred expenses.
- 2B. Reimburse its program \$129,872 from non-Federal funds for the interest paid on the line of credit.

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

- 2C. Consult with HUD's Office of General Counsel to determine the appropriateness of the Authority's using its fiscal year 2008 program funds to pay for the previously incurred expenses. If the use of the funds was not appropriate and should not be retroactively approved, the Authority should be required to reimburse its program \$1,417,421 from non-Federal funds for its fiscal year 2008 program award.

Finding 3: The Authority Failed To Comply With Federal Requirements and/or Its Own Procurement Policy

The Authority failed to comply with Federal requirements and/or its own procurement policy. Specifically, it did not (1) maintain records to support detailing significant procurement histories and (2) ensure that its maintenance staff and/or contractors were paid the appropriate Federal labor standards prevailing wage rates under the Davis-Bacon Act. The problems occurred because the former executive director disregarded Federal requirements. Additionally, the Authority's former board did not provide adequate oversight of the executive director's procurement activities. As a result, HUD lacked assurance that the Authority operated its program in an efficient manner, and the Authority owed more than \$49,000 in wage restitution.

The Authority's Did Not Maintain Procurement Records

The Authority did not maintain records to support its procurement activities. According to HUD's requirements at 24 CFR 85.36(b)(9), the local public housing agency must maintain sufficient procurement records to detail the significant history of a procurement. These records will include the rationale for the procurement method, contract type, and contractor selection and the basis for the contract price as required by HUD. Therefore, we obtained and reviewed 90 work orders that the Authority used to support charges to its 2007 and 2008 program.

The Authority's work order system was designed to account for all supplies used; purchase orders issued for materials, services, and equipment; and maintenance labor charges for the work order from employee timesheets. The work orders also contained the names of contractors and vendors who provided goods or services. Therefore, in reviewing the work orders, we identified 14 contractors that were paid \$198,000 collectively. Of the 14 contractors, 2 current maintenance employees were identified by the Authority's 2007 independent auditors.

One employee rented a large backhoe tractor to the Authority for \$10,850, and the other employee provided kitchen cabinets for 16 of the Authority's housing units for \$24,897. The cabinets were made during nonwork hours. For the remaining 12 contractors, 5 provided equipment only or were paid less than \$2,000, and 7 contractors provided services and were paid more than \$2,000. The following table provides a listing of the 12 contractors, the services provided, the number of work orders involved, and the total amount paid.

Contractor name	Service(s) provided	Number of work orders	Amount paid
*Jack Crowley Roofing	Roofing	11	\$97,782
*MJ Painting	Painting	28	20,079
*Elkins Tree Service	Tree trimming and removal	7	10,650
*D & H Glass Service	Window repair and reglazing	1	7,229
*Smiddy's Carpeting	Carpeting	5	6,477
*Double D Fence	Install fencing	2	3,385
HH Greg	Kitchen appliances	1	3,895
Indiana Wholesalers	Kitchen cabinets	1	3,174
*Chalos Carpet Cleaning	Clean unit	1	3,450
Crossroads Door	Custom steel entry door	1	1,315
Duncan Supply	Air conditioning unit	1	1,404
Elite View Windows	New replacement windows	1	647
Legend - *Davis-Bacon applicable			

As previously mentioned, the Authority was unable to support its procurement activities; therefore, we could not determine whether it complied with Federal requirements and its own procurement policy when procuring the goods and services identified above.

The Authority Did Not Comply With the Davis-Bacon Act

The Authority did not comply with the labor standards prevailing wage rates under the Davis-Bacon Act. For eight maintenance staff, three current and five former employees, who performed renovations to the Authority's office and residential housing units, the Authority did not pay them the appropriate wage rates. The employees were paid their regular wage rates instead of the wage rates in accordance with the Davis-Bacon Act. Therefore, based on the wage rates applicable during the time that the work was performed, the Authority owed the eight employees \$47,366 in wage restitution.

Since the Authority did not maintain records of its procurements, we were unable to determine, for the seven contractors identified above, whether the Authority informed them that Federal labor standards applied. HUD Handbook 1344.1, paragraph 2-7, requires public housing agencies' contract administrators and labor standards personnel to include the applicable wage determination in every construction contract and in bid documents when there is competitive bidding.

We randomly selected three contractors (Jack Crowley Roofing, MJ Painting, and D & H Glass Service) from which to obtain and review payroll records to determine whether their employees were paid the appropriate wage rate. We were unable to locate the owner of Jack Crowley Roofing; therefore, we were only able to review the payroll documentation for MJ Painting and D & H Glass Service. We determined that MJ Painting employees were paid the appropriate wage rates.

However, for D & H Glass Service, we identified three employees that were owed wage restitution of \$2,166.

HUD's Monitoring Review Identified the Authority's Davis-Bacon Violations

On May 15, 2002, HUD performed a monitoring review based on a complaint and determined that the Authority failed to apply Federal labor standards and Davis-Bacon wages appropriately for the construction and rehabilitation of its maintenance facility. The Authority also failed to notify its contractors of the labor standards provision and wages; therefore, there were many wage underpayments to employees. The Authority was required to obtain payrolls from all contractors, compute all hours worked by maintenance personnel on the project, and calculate the restitution owed to each employee based on the difference between what the employee was paid and the appropriate amount based on the wage decision. HUD required the Authority to provide its calculations and proof of restitution for review. In July 2002, the Authority paid \$95,516 in wage restitution for 43 employees, which included more than \$65,000 to its own maintenance staff. HUD's staff performed a follow-up monitoring visit in 2003 and did not identify any deficiencies.

Conclusion

The problems described above occurred because the former executive director disregarded Federal requirements. Further, the Authority's former board did not provide adequate oversight of the executive director's procurement activities. Although the Authority had a procurement policy, which stated that it would comply with Federal procurement requirements, it lacked procedures to aid its staff in implementing the policy. As a result, HUD lacked assurance that the Authority operated its program in an efficient manner.

Recommendations

We recommend that the Acting Director of HUD's Cleveland Office of Public Housing require the Authority to

- 3A. Reimburse its current and/or former maintenance employees and contractor \$49,532 (\$47,366 plus \$2,166) from non-Federal funds for wage restitution.
- 3B. Implement procedures and controls to aid in the implementation of its procurement policy.

- 3C. Maintain adequate records to support its procurement histories, such as bidding documentation, price analysis, etc., to ensure compliance with Federal requirements.
- 3D. Ensure that staff conducting its procurement activities is adequately trained and/or knowledgeable of Federal procurement requirements.
- 3E. Review the remaining five contractors identified in this finding to determine whether wage restitution is owed and provide the review results to HUD for approval. If wage restitution is required, the Authority should make the restitution from non-Federal funds.

Finding 4: The Authority Lacked Capacity To Adequately Expend Its Recovery Act Funds

The Authority lacked capacity to adequately expend its Recovery Act funds. It did not have (1) written policies and procedures governing the administration of its Recovery Act funds and (2) staff knowledgeable of HUD's and other Federal procurement requirements. The problems occurred because the previous board allowed the former executive director to control the Authority's financial and procurement activities without providing adequate oversight (see findings 1, 2, and 3) and the Authority's current executive director was not experienced in administering public housing programs. As a result, HUD had no assurance that the Authority had the necessary capabilities to manage its Recovery Act funding.

The Authority Lacked Capacity To Administer Its Recovery Act and Capital Fund Program Funds

The Authority obligated its Recovery Act funding in a timely manner. However, it lacked capacity to manage its Recovery Act funds. HUD's regulations at 24 CFR Part 903 require an approved annual public housing agency plan before program funds can be completely drawn down and expended. However, as of May 10, 2010, the Authority did not have an approved plan for 2009. HUD's Public and Indian Housing Notice 2009-12 states that the Authority must use its funds on capital fund-eligible activities currently identified in either the annual statement (a component of the annual plan) or 5-year action plan. The Authority's work items were included in its 5-year action plan. The Authority proposed using the funding to rehabilitate 16 vacant housing units at its Lockport and 40 housing units at its Market Avenue housing developments.

The Authority had not established policies and/or procedures for financial reporting, management controls, and procurement and monitoring (see finding 3), including the administration of its Recovery Act and Capital Fund Program funds. In October 2009, the Authority hired a financial management consulting firm, Asher PHA Finance, Limited Liability Corporation, to help it get its annual public housing plan and its five year plan approved by HUD. In January 2010, the Authority also contracted with the firm to prepare a cost allocation plan, assist with the development of financial management and internal control procedures, and provide training to its staff. The firm provided the Authority a policy and procedures guidebook which was approved by the Authority's board in May 2010. However, the policies and procedures guidebook did not address specific procurement, administrative, and reporting procedures.

Under the current executive director, the Authority did not have staff knowledgeable of HUD's procurement requirements and contract administration responsibilities for Federal programs. For instance, the Authority was unaware of

HUD's annual public housing agency plan preparation and submission process until December 2008. The Authority hired additional staff to increase its capacity to oversee its program, including the Recovery Act funds. However, the newly hired staff had no Federal procurement experience.

Conclusion

The problems described above occurred because the Authority's former board allowed the former executive director to have complete control over the Authority's operations without providing oversight (see findings 1, 2, and 3). In addition, under the current executive director, the Authority did not adopt policies and/or procedures for financial reporting, management controls, and procurement until May 2010. However, the policy and procedure guidebook did not address specific procurement, administrative, and reporting procedures. Further, the Authority's staff was not knowledgeable of Federal procurement requirements. The Authority has until March 17, 2011 to expend 60 percent of the Recovery Act funds.

Recommendation

We recommend that the Acting Director of HUD's Cleveland Office of Public Housing require the Authority to:

- 4A. Acquire capacity to manage its Recovery Act and other similar funding, including, but not limited to, staff persons knowledgeable in Federal procurement requirements or contracting for this expertise, developing specific procedures for financial reporting, management controls, and procurement.

SCOPE AND METHODOLOGY

To accomplish our objectives, we reviewed

- Applicable laws and regulations; the Authority's contract; HUD's program requirements at 24 CFR Parts 85, 903, and 965; the Authority's financial and accounting records, annual audited financial statements from 2006 to 2008, general ledgers from 2007 through 2009, bank statements, check registers, accounting spreadsheets, policies and procedures, by-laws, board meeting minutes, organizational charts, correspondence with HUD, annual plans for fiscal years 2000 through 2009, and modernization activity documentation (maintenance work orders, purchase orders, invoices); and other related documentation.
- The Authority's construction loan documents (purchase agreement between the finance company and the Authority; a facility resource planning agreement between the contractor and the Authority; and an escrow agreement among the finance company, the Authority, and the escrow agent) and a cost proposal for the Dreiser Square elderly project.
- HUD's files for the Authority.
- The Authority's line of credit agreements and other related bank documents.
- The U.S. Department of Labor wage determinations in effect during our review period.

We also interviewed the Authority's current and former employees; current and former board of commissioners; HUD staff; the Authority's consultants; and representatives from First Financial Bank, Hawkins, Ashe, and Baptie & Company, MJ Painting, D & H Glass Service, and Myszak and Palmer, Architects.

We performed our onsite audit work between June 2009 and January 2010. The audit covered the period October 1, 2007, through May 31, 2009. The period was extended as necessary.

We reviewed the Authority's construction loan that was obtained in 1999 because the Authority's new executive director expressed concerns about the loan, and the Authority was still making payments on the loan in 2008. In reviewing the Authority's program, we determined that the Authority regularly obtained private financing for its capital improvements, as evidenced by its bank line of credit.

We conducted our 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are achieved:

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. They 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 objectives:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Relevance and reliability of information – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with applicable laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

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

- The Authority lacked adequate procedures and controls to ensure that it complied with its contract and Federal requirements (see findings 1, 2, and 3).
- The Authority lacked the capacity to administer its Recovery Act and Capital Fund Program funds (see finding 4).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/	Unsupported 2/
1B	\$861,756	
1D		\$2,419,847
2B	129,872	
2C		<u>1,417,421</u>
3A	<u>49,532</u>	
Totals	<u>\$1,041,160</u>	<u>\$3,837,268</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.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

HOUSING AUTHORITY OF THE CITY OF TERRE HAUTE

Board of Commissioners

JOHN WOLF TERESA PRINCE JEFF HARPOLE
TOM HUNT PATRICIA PARKER-ZAIKOVSKY MARSHALL RECTOR

June 18, 2010

VIA FIRST CLASS MAIL AND EMAIL

Ms. Kelly Anderson, Assistant Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General
77 West Jackson Boulevard, Suite 2646
Chicago, IL 60604

**RE: Management Comments to Discussion Draft Audit Report 2010-
CH-101X (Public Housing Capital Fund Program)**

Dear Ms. Anderson,

On behalf of the Housing Authority of the City of Terre Haute (the "Authority"), I am writing to provide the Authority's comments to the discussion draft audit report from the Office of Inspector General (the "OIG") relating to the Authority's public housing capital fund program. I note from the outset that the ostensible objectives of the audit were "to determine whether the Authority (1) properly administered its program and (2) had the capacity to administer its Recovery Act funds." In spite of these stated objectives, the audit reached back over a decade to set forth findings that are wholly unrelated to the American Recovery and Reinvestment Act of 2009 (the "Recovery Act") as well as to the Authority's present capacity to administer Recovery Act funds. In fact, the audit focused almost exclusively on actions taken years ago by a previous administration, and then attempts to extrapolate the findings to apply to the current administration. Thus, the audit reaches several illogical conclusions which are detailed more fully herein.

The following are our comments on each of the findings and recommendations:

Finding 1: The Authority Obtained a \$2.3 Million Construction Loan by Encumbering Project Assets Contrary to Its Contract with HUD

Recommendations

P.O. BOX 3086 TERRE HAUTE, INDIANA 47803-0086
812-232-1381 812-234-4164 (FAX) 800-545-1833, ext. 271 (TDD)

Comment 1

Ref to OIG Evaluation

Auditee Comments

Comment 2

Authority's Response: Disagree. The OIG is aware that the current administration of the Authority is unable to produce documents from over a decade ago. Neither the federal regulations (*See* 24 C.F.R. §84.53), nor state law, nor the Authority's document retention policy requires the retention of such records for that period of time.

Further, the prior executive director was employed at the Indianapolis Field Office prior to his tenure at the Authority and would have been well aware of HUD requirements and guidelines. While the Authority no longer has the records at issue, HUD may have the records in its files.

1B. Reimburse HUD \$791,650 for the interest incurred on the loan from 2000 to 2007 and reimburse its project \$70,106 for the interest incurred on the loan after October 2008 from non-Federal funds.

Comment 3

Authority's Response: Disagree. It is unquestioned that the loan funds were used for the purpose of supporting the low income housing program. All of the upgrades performed using the loan funds were appropriate expenditures and would have been entirely permissible had they been paid for from the annual capital fund allocation. To require the Authority to reimburse interest on the loan would lead to the inequitable result that the Authority would pay twice for the same work, while HUD gained the benefit of the work originally performed. Reimbursement of interest should not be required.

Comment 4

Moreover, pursuant to OMB Circular A-87, interest on borrowed capital for financing otherwise allowable costs is permitted in certain instances, including a construction loan such as the one at issue here. There is no reasonable correlation between the demand for repayment of interest and the alleged error (the absence of HUD approval).

Comment 5

Given the foregoing, in lieu of repayment of interest we suggest that the Authority be required to develop policies and procedures to ensure that assets are not encumbered without appropriate HUD approval.

That the Director of HUD's Cleveland Office of Public Housing:

1C. Inform the Acting Deputy Assistant Secretary for Field Operations of the Authority's actions, which may result in a substantial default of its contract.

Authority's Response: Disagree. As discussed during the exit conference, the Authority believes that this recommendation should be revised to read: "Inform the Acting Deputy Assistant Secretary for

Ref to OIG Evaluation

Auditee Comments

Comment 6

Field Operations of the Authority's actions." In this way, the parties can provide for proper policies and procedures henceforth. The failure of the Authority, if any, was not obtaining HUD approval. The actual expenditure has not been questioned. To suggest that a substantial default which allegedly occurred over a decade ago be punished now is not logical and does nothing to facilitate the provision of safe, decent, and sanitary public housing today.

1D. Consult with HUD's Office of General Counsel to determine whether the loan encumbered and/or pledged the Authority's project assets. If the loan only encumbered the assets, a determination is needed regarding whether the loan can be retroactively approved (see recommendation 1A). If the loan cannot be approved, the Authority should be required to reimburse its program \$1,616,973 and its project \$802,874 from non-Federal funds. The funds due to the project should be deposited into the project's restricted operating reserve.

Authority's Response: Disagree. It is unquestioned that the loan funds were used for the purpose of supporting the low income housing program. All of the upgrades performed using the loan funds were appropriate expenditures and would have been entirely permissible had they been paid for from the annual capital fund allocation. To require the Authority to reimburse principal on the loan would lead to the inequitable result that the Authority would pay twice for the same work, while HUD gains the benefit of the work originally performed. Reimbursement should not be required. Instead, we suggest that the Authority be required to develop policies and procedures to ensure that assets are not encumbered without appropriate HUD approval.

**Comment 3
and 5**

That the Director, in conjunction with the Director of HUD's Departmental Enforcement Center:

1E. Pursue the appropriate administrative sanction(s) against the Authority's former executive director for failing to enforce HUD's requirements.

Authority's Response: Agree.

That HUD's Associate General Counsel for Program Enforcement:

1F. Determine legal sufficiency, and if legally sufficient, pursue remedies under the Program Fraud and Civil Remedies Act against the Authority's former board chairperson/principals for incorrectly

Ref to OIG Evaluation

Auditee Comments

Comment 7

certifying that the information contained in the Authority's annual plans was true and accurate when it was not.

Authority's Response: Disagree. The strength of character of the previous Board chairperson is the sole reason that the Authority was able to disengage and sever ties with the previous executive director, under whose watch all of the malfeasance alleged in the audit report allegedly occurred. Additionally, blame should be placed on all of the auditors who performed the annual audits over the last decade, yet never identified any of the issues found by the OIG's audit team. While we agree that certain remedies should be required, we believe that those should be demanded from the prior auditors, not the prior Board.

Finding 2: The Authority Encumbered Project Assets When It Obtained a Bank Line of Credit to Finance Capital Improvements

Recommendations

That the Director of HUD's Cleveland Office of Public Housing require the Authority to:

2A. Provide documentation to support that HUD approved the line of credit and the use of program funds for reimbursement of previously incurred expenses.

Comment 8

Authority's Response: Disagree. The OIG is aware that the current administration of the Authority is unable to produce documents from over a decade ago. Neither the federal regulations (*See* 24 C.F.R. §84.53), nor state law, nor the Authority's document retention policy requires the retention of such records for that period of time.

Further, the prior executive director was employed at the Indianapolis Field Office prior to his tenure at the Authority and would have been well aware of HUD requirements and guidelines. While the Authority no longer has the records at issue, HUD may have the records in its files.

2B. Reimburse its program \$129,872 from non-Federal funds for the interest paid on the line of credit.

**Comment 3
and 4**

Authority's Response: Disagree. It is unquestioned that the line of credit was used for the purpose of supporting the low income housing program. All of the capital improvements made using funds from the line of credit were appropriate expenditures and would have been

Comment 9

entirely permissible had they been incurred and paid for from the same year's annual capital fund allocation. To require the Authority to reimburse interest on the line of credit would lead to the inequitable result that the Authority would pay twice for the same work, while HUD gains the benefit of the work originally performed. Reimbursement of interest should not be required.

Moreover, pursuant to OMB Circular A-87, interest on borrowed capital for financing otherwise allowable costs is permitted in certain instances, including a line of credit to finance capital improvements such as the one at issue here. There is no reasonable correlation between the demand for repayment of interest and the alleged error (the absence of HUD approval).

Given the foregoing, in lieu of repayment of interest we suggest that the Authority be required to develop policies and procedures to ensure that assets are not encumbered without appropriate HUD approval.

That the Director of HUD's Cleveland Office of Public Housing:

2C. Consult with HUD's Office of General Counsel to determine the appropriateness of the Authority's using its fiscal year 2008 program funds to pay for the previously incurred expenses. If the use of the funds was not appropriate and should not be retroactively approved, the Authority should be required to reimburse its program \$1,417,421 from non-Federal funds for its fiscal year 2008 program award.

Authority's Response: Disagree. Again, it is unquestioned that the program funds in question were used for the purpose of supporting the low income housing program even if they were used to satisfy previously incurred expenses under the line of credit. All of the capital improvements made using funds from the line of credit were appropriate expenditures and would have been entirely permissible had they been incurred and paid for from the same annual capital fund allocation. To require the Authority to reimburse interest on the line of credit would lead to the inequitable result that the Authority would pay twice for the same work, while HUD gains the benefit of the work originally performed. Reimbursement of interest should not be required. Instead, we suggest that the Authority be required to develop policies and procedures to ensure that program funds are used for their intended purposes.

Finding 3: The Authority Failed To Comply With Federal Requirements and/or Its Own Procurement Policy

Ref to OIG Evaluation

Auditee Comments

Comment 10

Comment 11

Comment 12

Recommendations

That the Director of HUD's Cleveland Office of Public Housing require the Authority to:

3A. Reimburse its current and/or former maintenance employees and contractor \$49,369 (\$47,203 plus \$2,166) from non-Federal funds for wage restitution.

Authority's Response: Disagree. To the extent that employees of contractors were not paid appropriately in accordance with the applicable prevailing wage standards, restitution should be paid to them by their employer, not the Authority. There is no assertion that the Authority breached the contracts with either of the contractors reviewed (MJ Painting and D&H Glass Service), or that they were not paid in full for their work. Accordingly, the burden of making those employees "whole", if such a burden exists, should fall to their employers. To require the Authority to pay the wage restitution would lead to the inequitable result that the Authority would pay twice for the same work, having paid the contractors in full once already. Instead, we suggest that HUD's Office of Labor Relations undertake audits of the contractors at issue and determine whether they owe wage restitution to their employees, taking into consideration the two-year statute of limitation for wage claims by the employees.

To the extent that employees of the Authority were not paid appropriately in accordance with the applicable prevailing wage standards, the Authority will consider paying wage restitution provided that the employees' claims for the wages are not time barred by the applicable two-year statute of limitations.

3B. Implement procedures and controls to aid in the implementation of its procurement policy.

Authority's Response: Agree. The Authority has taken and continues to take steps to implement best practices procedures and controls with respect to the implementation of its procurement policy.

3C. Maintain adequate records to support its procurement histories, such as bidding documentation, price analysis, etc., to ensure compliance with Federal requirements.

Authority's Response: Agree. The Authority has taken and continues to take steps to implement best practices procedures and controls with

Comment 10

respect to procurement activities to ensure compliance with all Federal requirements.

3D. Ensure that staff conducting its procurement activities is adequately trained and/or knowledgeable of Federal procurement requirements.

Authority's Response: Agree. The Authority has taken and continues to take steps to train staff to ensure compliance with all Federal requirements.

3E. Review the remaining five contractors identified in this finding to determine whether wage restitution is owed and provide the review results to HUD for approval. If wage restitution is required, the Authority should make the restitution from non-Federal funds.

Authority's Response: Disagree. To the extent that employees of contractors were not paid appropriately in accordance with the applicable prevailing wage standards, restitution should be paid to them by their employer, not the Authority. There is no assertion that the Authority breached the contracts with any of the remaining five contractors, or that they were not paid in full for their work. Accordingly, the burden of making those employees "whole", if such a burden exists, should fall to their employers. To require the Authority to pay the wage restitution would lead to the inequitable result that the Authority would pay twice for the same work, having paid the contractor in full once already. Instead, we suggest that HUD's Office of Labor Relations undertake audits of the contractors at issue and determine whether they owe wage restitution to their employees, taking into account the two-year statute of limitation for wage claims by the employees.

Finding 4: The Authority Lacked Capacity to Adequately Expend Its Recovery Act Funds

Recommendations

That the Director of HUD's Cleveland Office of Public Housing require the Authority to:

4A. Require an alternate third-party entity to manage the Authority's Recovery Act funds based on the Authority's prior mismanagement of its program and lack of policies and/or procedures for financial reporting, management controls, and procurement.

Ref to OIG Evaluation

Auditee Comments

Comment 13

Authority's Response: Disagree. It is unquestionable that the alleged prior mismanagement occurred on the watch of the prior administration of the Authority. This finding and recommendation asserts that the Authority continues to be managerially incapable of administering the Recovery Act funds. There is simply no support for that contention. While the Authority's new administration acknowledges a learning curve to gain knowledge about reporting issues and to become fully compliant, significant steps have been taken in that regard. Where necessary, consultants have been retained to advise and to train the Authority's staff. The auditors were fully aware that Asher PHA Finance, LLC has been retained since October 2009, (not January 2010 as the audit asserts), to assist the Authority with all financial issues. Legal counsel, Cohen & Grigsby, PC, was retained in April 2010 to assist the Authority with compliance and audit issues. Further, the additional staff that have been hired to increase the Authority's capacity to oversee its program have gone or are undergoing training, both on the job and through other providers.

Most significantly, there is no support for the contention that the Authority "lacked capacity to adequately expend its Recovery Act funds." The Authority's Recovery Act funds were obligated, as required, by March 17, 2010. While the audit correctly states that various required policies and procedures were not adopted by May 10, 2010, the audit fails to acknowledge that those policies and procedures were duly approved by the Authority Board at their regular meeting on May 27, 2010. To penalize the Authority because the Board meeting falls at the end of the month, rather than the beginning, is punitive.

The Authority has obligated the Recovery Act funds to rehabilitate 16 vacant housing units at its Lockport development and 40 housing units at its Market Avenue Development and sees no obstacles at this time to expending 60% of the Recovery Act funds by the March 17, 2011 deadline.

Finally, as a troubled agency, the Field Office has been responsible for approving the Authority's obligation and expenditure of funds at every step of the way. Simply stated, funds cannot be spent without HUD approval which creates an effective check-and-balance system to ensure that the Authority is spending funds appropriately.

The Authority proposes that an alternate remedy to this finding is for the Cleveland Office of Public Housing to provide the Authority with

Ref to OIG Evaluation

Auditee Comments

Comment 14

sufficient technical assistance, when requested, to aid the Authority to comply fully with all Recovery Act requirements.

The audit accomplishes one thing particularly well in that it notes repeatedly the deficiencies of the prior administration. Missing from the audit, however, is any suggestion that HUD and others bear some responsibility for essentially being "asleep at the wheel" during a decade of mismanagement at the Authority. While it is reasonable to believe that HUD and the Authority's auditors surmised that the executive director, as their former employee, was capable and competent to manage the agency, that was clearly not the case. If anything, the appearance of power and authority that the prior executive director wielded based on his HUD experience proved to be one of the biggest obstacles to severing him from his position and starting the process of repairing the agency.

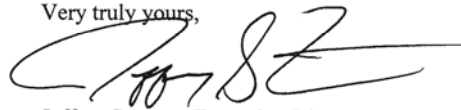
Comment 15

As with the three earlier audit reports and their findings and recommendations, while the Authority agrees with certain findings in this discussion draft audit report, we do not agree with all of them. We also note that if the recommendations in the discussion draft are not revised, to at least eliminate the inequity of multiple payments for the same work, and thus become the final recommendations, the resulting \$4,878,265.00 in suggested reimbursements from this audit alone could financially devastate the agency and put an immediate end to the tremendous progress that has been made by the new administration.

Comment 16

The Authority certainly understands and acknowledges the need for public accountability and full compliance with all applicable laws. We believe, however, that the suggested remedies set forth in the draft discussion audit are so disconnected from the alleged failures that led to the findings so as to be punitive and ultimately damaging to the Authority in a manner out of proportion to the underlying errors. Our hope is that you will reconsider both the four findings and the numerous recommendations in light of these comments.

Very truly yours,



Jeffrey Stewart, Executive Director

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cc: Sandra B. Henriquez, Assistant Secretary for Public & Indian Housing
Heath Wolfe, Regional Inspector General for Audit
Michael H. Syme, Esq.

OIG Evaluation of Auditee Comments

- Comment 1** Although the issues cited in findings 1, 2, and 3 in our discussion draft audit report occurred under the previous administration, they should be corrected for the current administration to move forward in the right direction. Further, the current administration is responsible for ensuring that the Authority complies with its contract with HUD, regardless of when the issues occurred, since it is overseeing the operations of the same entity.
- Comment 2** HUD's regulations at 24 CFR, part 84.53, on uniform administrative requirements for grants applies to nonprofit organizations. HUD's requirements at 24 CFR, part 85, on uniform administrative requirements for grants applies to state and local governments. However, both requirements on records retention state that the retention period for financial records, supporting documents, statistical records, and all other records pertinent to an award shall be kept for a period of three years from the date of submission of the final expenditure report or annual financial report. The Authority's final expenditure on the construction loan was December 2009 so the final expenditure report or annual financial report pertinent to this contract would be the annual financial report for the year ended September 30, 2010. Therefore, the record retention period has not expired.
- Comment 3** The Authority did not follow proper procedures and should have provided the necessary documentation to HUD to show that the electrical upgrades at Dreiser Square were appropriate expenditures. This would have provided HUD the opportunity to determine the appropriateness of the project and to ensure HUD's and the Authority's interests were safeguarded. However, since the former executive director obtained a project loan that placed a lien on the Authority's project assets without HUD's approval; HUD has no assurance that all of the upgrades were appropriate. Further, HUD specifically requires public housing agencies, under its contract, to request prior approval before entering into any loan agreements that encumbers any assets of the Authority that are covered by its contract with HUD. Since the Authority did not seek HUD approval, interest costs on the project loan are ineligible to be paid with Federal funds.
- Comment 4** According to the Office of Management and Budget's Circular A-87, attachment B, section 23(a), costs incurred for interest on borrowed capital or the use of a government unit's own funds, however represented, are unallowable except as specifically provided in subsection b or authorized by Federal legislation. Since HUD requires an authority, under its contract, to request prior approval before entering any loan agreements that encumbers any assets of the Authority that are covered by its contract, any interest costs without HUD's approval are considered unallowable.
- Comment 5** The Authority already has a policy in place to prevent the encumbrance of assets without the appropriate HUD approval, which is its contract with HUD. Therefore, the recommendations proposed in this audit report are appropriate.

- Comment 6** We disagree. Recommendation 1C in our discussion draft audit report is appropriate considering the issues cited in this report. Although the issues identified for finding 1 occurred under the prior administration, it does not negate that these actions possibly resulted in the Authority substantially defaulting on its contract with HUD.
- Comment 7** Violations of HUD's requirements are subject to administrative actions, including referral for remedies under the Program Fraud Civil Remedies Act. Further, HUD form 50077 cited in our discussion draft audit report clearly warns that HUD will pursue false claims and statements. Therefore, our recommendation is appropriate. The discussion audit report addressed the actions of the Authority not its prior auditors. Therefore, any discussion of actions, if any, against the prior auditors should not be addressed in this report.
- Comment 8** The Authority's last expenditure occurred in 2009; therefore, the record retention period has not expired. See comment 2.
- Comment 9** See comments 3 and 4. Although finding 2 in our discussion draft audit report does not include a recommendation for the Authority to develop policies and procedures to ensure that program funds are used for their intended purposes, the recommendation is included in finding 4. Recommendation 2C will remain due to the issues identified in this audit report.
- Comment 10** HUD requirements established that authorities are responsible for the administration and enforcement of labor standards in Federally-funded or assisted projects. Failure by the Authority to include the wage determinations in bid documents and contracts does not relieve it of the responsibility for enforcement action. Since the Authority did not notify the bidders and contractors of Davis-Bacon labor standards in its bid documents and contracts, and did not monitor for compliance with Davis-Bacon wage rates, it is the Authority's responsibility and not the contractors to make those employees whole. It should be noted that not all Authority business with contractors involve the payment of Davis-Bacon Act wage rates. Therefore, it is the responsibility of the Authority to notify potential bidders when Davis-Bacon Act labor standards apply.
- Comment 11** As previously stated, it is the Authority's responsibility for the administration and enforcement of labor standards in Federally-funded or assisted projects. Therefore, it should determine whether contractors are owed wage restitutions. The two year statute of limitation for wage claims refers to employee claims under the Fair Labor Standards Act. However, the Authority is responsible for notifying contractors of Davis-Bacon labor standards in its bid documents and contracts, and monitoring for compliance with the Davis-Bacon wage rates.
- Comment 12** The Authority indicated a willingness to consider wage restitution provided that the two year statute of limitation for wage claims is not applicable. HUD requires

that all maintenance and laborers employed for the operation of public housing must be paid no less than the prevailing wages determined or adopted by HUD.

Comment 13 We commend the Authority for the significant steps it has undertaken to improve its operations. Although some changes have been made, improvements are still needed. Nonetheless, we have revised our recommendation in consideration of the steps undertaken made by the Authority to improve its operations.

Comment 14 The Authority's board is primarily responsible for the actions of the Authority. It is the Authority responsibility to provide information to HUD; therefore, failure to provide accurate and complete information obstructs HUD's ability to properly monitor.

Comment 15 We disagree. The amounts cited in our discussion draft audit report do not constitute payments for the same work. The report clearly identifies the costs charged and the sources of funding, when appropriate, that comprised the figures contained in the report. Based on the issues identified in our audit report, we made the appropriate recommendations to HUD.

Comment 16 Although the issues cited in findings 1, 2, and 3 in our discussion draft audit report occurred under the previous administration, they should be corrected for the current administration to move forward in the right direction. Therefore based on the issues identified in the report, we made the appropriate recommendations to HUD. The Authority has opportunity to work with HUD to resolve the recommendations.

Appendix C

FEDERAL REQUIREMENTS

Section 7 of the Authority's contract with HUD states that the Authority shall not pledge as collateral for a loan assets of any project covered under this contract.

Section 17 of the contract states that events of substantial default shall include but shall not be limited to any of the following occurrences: (1) failure to maintain and operate the project(s) under this contract in decent, safe, and sanitary manner and (2) the disposition or encumbrance of any project or portion thereof without HUD approval.

HUD's regulations at Title 24, Code of Federal Regulations, Part 85.22 (*24CFR Part 85.22*) requires the Housing Authority to comply with the cost principles in Office of Management and Budget Circular, A-87. Attachment B, Section 23(a) of this circular on "interest" states: "Costs incurred for interest on borrowed capital or the use of a governmental unit's own funds, however represented, are unallowable except as specifically provided in subsection b or authorized by federal legislation. Subsection b applies to financing costs (including interest) paid or incurred which are otherwise associated with allowable costs of building acquisition, construction, rehabilitation or remodeling. HUD requires public housing agencies under its contract to request prior approval before entering any loan agreements that encumbers any assets of the public housing agency that are covered by its contract.

HUD's regulations at 24 CFR Part 903.7(c) require that annual plans include a statement of financial resources. This statement must address the financial resources that are available to the public housing agency for the support of Federal public housing and tenant-based assistance programs administered by the authority during the plan year. The statement must include a listing, by general categories, of the authority's anticipated resources, such as its operating, capital and other anticipated Federal resources available to the authority, as well as tenant rents and other income available to support public housing or tenant based assistance. The statement also should include the non-Federal sources of funds supporting each Federal program, and state the planned uses for the resources.

HUD's regulations at 24 CFR Part 965.302 requires all public housing agencies to complete an energy audit for each housing project it owns under management at least once every five years. Further, 24 CFR Part 965.402 states that a cost benefit analysis shall be made to determine whether a change to individual metering will be cost effective.

The Contract Amendments for the Capital Fund Program (CFP) (Form HUD-53012) between HUD and the Authority (herein called the PHA), paragraph 3 states in part:

"...the 24 month time period in which the PHA must obligate this CFP assistance pursuant to Section 9(j) (1) of the United States Housing Act of 1937, as amended, and the 48 month time period in which the PHA must expend its CFP assistance pursuant to Section 9(j) (5) of the Act

starts with the effective date of this CFP assistance (the date on which CFP assistance becomes available to the PHA for obligation.)”

HUD’s regulations at 2 CFR 2424.10 state that HUD adopted, as HUD’s policies, procedures, and requirements for nonprocurement debarment and suspension, the Federal regulations at 2 CFR Part 180.

HUD’s regulations at 24 CFR 24.1 state that the policies, procedures, and requirements at 2 CFR Part 2424 permit HUD to take administrative sanctions against employees of recipients under HUD assistance agreements that violate HUD’s requirements. The sanctions include debarment, suspension, or limited denial of participation and are authorized by 2 CFR 180.800, 2 CFR 180.700, or 2 CFR 2424.1110, respectively. HUD may impose administrative sanctions based upon the following conditions:

- ❖ Failure to honor contractual obligations or to proceed in accordance with contract specifications or HUD regulations (limited denial of participation);
- ❖ Violation of any law, regulation, or procedure relating to the application for financial assistance, insurance, or guarantee or to the performance of obligations incurred pursuant to a grant of financial assistance or pursuant to a conditional or final commitment to insure or guarantee (limited denial of participation);
- ❖ Violation of the terms of a public agreement or transaction so serious as to affect the integrity of an agency program, such as a history of failure to perform or unsatisfactory performance of one or more public agreements or transactions (debarment); or
- ❖ Any other cause so serious or compelling in nature that it affects the present responsibility of a person (debarment).