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Office of Inspector General for Audit, Region V
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MEMORANDUM NO.
2010-CH-1803

February 25, 2010

MEMORANDUM FOR: Robert F. Poffenberger, Director of Community Planning and Development, 5HD


FROM: Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: The State of Indiana's Administrator Awarded Neighborhood Stabilization Program Funds for an Inappropriate Project

INTRODUCTION

We reviewed the State of Indiana's (State) Neighborhood Stabilization Program (Program). The review was part of the activities in our fiscal year 2010 annual audit plan. We selected the State based upon a citizen's complaint to our office. Our objective was to determine whether the State awarded Program funds to eligible projects.

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

METHODOLOGY AND SCOPE

To accomplish our objective, we reviewed

- Applicable laws; the Federal Register, dated October 6, 2008, May 4, 2009, and June 19, 2009; HUD's regulations at 24 CFR (Code of Federal Regulations) Part 570; and HUD's Program grant agreement with the State.
- The State's 2008 consolidated plan substantial amendment for the Program and data from HUD's Disaster Recovery Grant Reporting system.
- The Indiana Housing and Community Development Authority's (Authority) accounting records, annual audited financial statements for 2008, project files, policies and procedures, board meeting minutes, organizational chart, and grant

agreements with recipients; recipients' applications; and action plan submitted to HUD regarding the City of Mishawaka, IN.

We also interviewed the Authority's employees, recipients' employees, and HUD's staff.

We reviewed the following two projects identified in the complaint: the City of Mishawaka's redevelopment of the Mishawaka Furniture building and the City of Lafayette, IN's redevelopment of the Bridgeway Apartment Complex. We also reviewed applications and/or grant agreements for the remaining 22 local entities that were awarded Program funds to determine whether they planned to use the funds for the redevelopment of commercial buildings. The applications and/or grant agreements for 20 of the local entities did not include the use of Program funds for the redevelopment of commercial buildings. The applications for the two remaining local entities included projects that could involve the use of Program funds for the redevelopment of commercial buildings. The application for Dubois-Pike-Warrick Economic Opportunity Committee, Inc., doing business as TRI-CAP, included the redevelopment of buildings for up to three units of single-family scattered-site housing. TRI-CAP identified 14 potential sites which could be used for the single-family scattered-site housing. Nine of the sites were commercial buildings. The application for Southeast Neighborhood Development, Inc. included the acquisition and rehabilitation or demolition of 25 buildings. The application stated that Southeast Neighborhood Development, Inc. had identified 19 buildings that it could acquire and included a map with 20 property addresses. One of the properties was a commercial building. However, the application did not state which buildings would be rehabilitated and which buildings would be demolished.

We performed our on-site review work from October through December 2009 at the Authority's office located at 30 South Meridian Street, Indianapolis, IN. The review period was October 2008 through September 2009 and was expanded as determined necessary.

We did not perform our review in accordance with generally accepted government auditing standards. We designed the review to be proactive and focus on prevention. Therefore, we significantly reduced the scope of our review. These facts do not affect the significance of the conditions identified in this memorandum.

BACKGROUND

The Program. Authorized under Title III of the Housing and Economic Recovery Act of 2008 (Act), as amended, the Program provides grants to every State and certain local communities to purchase foreclosed-upon or abandoned homes and to rehabilitate, resell, or redevelop these homes to stabilize neighborhoods and stem the decline in value of neighboring homes. HUD allocated more than \$3.9 billion in Program funds to grantees.

The State. The Authority administers the State's Program. The Authority was created in 1978 by the Indiana General Assembly and is a quasi-public financially self-sufficient statewide government agency. It is governed by a seven-member board of commissioners (board) consisting of the State's lieutenant governor, the State's treasurer, and the Indiana Finance Authority's public finance director. The board includes four other members appointed to 4-year

terms by the State's governor. Its mission is for every resident of the State to have the opportunity to live in safe, affordable, good-quality housing in economically stable communities. The Authority's records are located at 30 South Meridian Street, Indianapolis, IN.

HUD allocated nearly \$83.8 million in Program funds to the State based upon the funding formula developed by HUD pursuant to the Act. On March 23, 2009, HUD entered into a grant agreement with the State for the full amount allocated. The Authority awarded nearly \$61.2 million of the funds to 24 local entities for comprehensive community revitalization and neighborhood redevelopment in areas of greatest need and set aside nearly \$22.6 million of the funds for a revolving loan fund to provide income-qualified individuals and families downpayment assistance to purchase foreclosed-upon homes in the areas of greatest need. Further, the Authority is reallocating \$15 million set aside for the revolving loan fund and awarding it to local entities for comprehensive community revitalization and neighborhood redevelopment in areas of greatest need.

HUD also awarded the State more than \$38 million in Tax Credit Assistance Program funds, nearly \$16.9 million in Homelessness Prevention and Rapid Re-Housing Program funds, and nearly \$8.4 million in Community Development Block Grant funds pursuant to the American Recovery and Reinvestment Act of 2009 (Recovery Act). The Authority also administered the State's Tax Credit Assistance and Homelessness Prevention and Rapid Re-Housing Programs. The State submitted an application for but did not receive Program funding pursuant to the Recovery Act.

RESULTS OF REVIEW

The State's Administrator Awarded \$4.5 Million in Program Funds for an Inappropriate Project

The Federal Register, dated October 6, 2008, stated that the eligible uses for Program funds included the following: the establishment of financing mechanisms for the purchase and redevelopment of foreclosed-upon homes and residential properties, including such mechanisms as soft-second, loan-loss reserves, and shared-equity loans for low- and moderate-income homebuyers; the purchase and rehabilitation of homes and residential properties that have been abandoned or foreclosed upon to sell, rent, or redevelop such homes and properties; the establishment of land banks for homes that have been foreclosed upon; demolition of blighted structures; and the redevelopment of demolished or vacant properties.

Contrary to HUD's requirements, the Authority awarded \$4.5 million in Program funds to the City of Mishawaka to redevelop the Mishawaka Furniture building, a commercial building located at 402 Lincoln Way West, Mishawaka, IN. Since the project involved the redevelopment of a commercial building, it would only qualify as an eligible Program project if the Mishawaka Furniture building was vacant. However, the building was not vacant and the Mishawaka Furniture Corporation, Inc. (Corporation) was conducting its operations from the building as of December 2009.

On March 3, 2009, the City of Mishawaka entered into a buy-and-sell agreement with Mishawaka Old School Properties, LLC (Properties) to purchase the Mishawaka Furniture building for nearly \$567,000. Section 10 of the buy-and-sell agreement stated that the City shall afford Properties an

opportunity to lease the property for a period not to exceed 9 months from the date of closing to allow the seller to close and relocate from the premises. The lease agreement, if desired, shall be executed at the time of closing. If the Program funds were not obtained in whole by June 21, 2009, the buy-and-sell agreement shall be considered null and void, except when mutually agreed to and accepted by both the City and Properties. Closing was intended to occur within 30 days of the City receiving notification that it would receive the Program funds.

On March 13, 2009, the City of Mishawaka applied for \$6.5 million in Program funds to create 52 residences for low- to moderate-income households, which included the conversion of the Mishawaka Furniture building into 32-affordable rent senior citizen apartments using \$4.5 million in Program funds. Section IV of the application described the conversion of the building under the heading “redevelop vacant properties.” Section VI of the application stated that the City did not own the building but entered into the buy-and-sell agreement with the current owners of the building contingent upon being awarded the Program funds. The City provided the buy-and-sell agreement with its application to the Authority. However, the Authority’s neighborhood stabilization manager stated that the Authority was not aware that the City would lease the building after its purchase.

On May 28, 2009, the Authority informed the City of Mishawaka that it had approved the City’s application for the \$6.5 million in Program funds. On July 27, 2009, the City purchased the Mishawaka Furniture building from Properties with non-Federal funds. The City entered into a commercial lease agreement with the Corporation to use the building as a furniture store on a month-to-month basis not to exceed 7 months, beginning July 13, 2009, and ending February 13, 2010. On September 3, 2009, the Authority entered into a grant agreement with the City effective July 1, 2009, for \$6.5 million in Program funds for eligible costs of the projects described in the City’s March 13, 2009, application.

As illustrated on the following page, an advertisement from the December 8, 2009, edition of the South Bend Tribune showed that the Corporation was conducting its operations from the Mishawaka Furniture building as of December 2009.

FINAL WEEKS!

Mishawaka
**FURNITURE
 STORE CLOSING
 LIQUIDATION**

**The Building
 Is SOLD!**

**We Must
 SELL-OUT to
 MOVE OUT**

**PRICES
 SLASHED
 AGAIN!** up to **70%
 OFF
 AND EVEN
 MORE!**

YOUR CHOICE
**Thousands Of Furniture
 Items To Choose From**
New Shipments from Warehouse!

*Hurry! You Just Can't Buy
 This Kind Of Quality For Less!*
 SOFAS, TABLES, LAMPS, PICTURES,
 RECLINERS, CHAIRS, DINING ROOMS,
 CHINAS, BUFFETS, BEDROOMS, CHEST,
 MIRRORS, DRESSERS, MATTRESSES,
 MEDIA CABINETS, DESKS, CURIOS,
 CABINETS, PAINTINGS, PLANTS, HOME
 ACCENTS AND MUCH MORE!

Plus!
**0% INTEREST
 FINANCING**

**EVERYTHING MUST BE SOLD! REGARDLESS OF OUR COST OR LOSS!
 HURRY! AT THESE PRICES.... THE BEST WILL GO FAST!**

402 Lincoln Way West - Mishawaka
574.259.5494
 Mon-Thurs - Fri 10-8 • Tues-Wed-Sat 10-6 • Sun Noon-6

In addition, as of December 28, 2009, the Corporation's Web site for the store stated that the Mishawaka Furniture building had been purchased by the City of Mishawaka and the Corporation must vacate the premises by February 2010.

The Authority lacked adequate procedures and controls to ensure that it awarded Program funds for eligible projects. It did not thoroughly review the City of Mishawaka's application for Program funds and the Mishawaka Furniture building to ensure that the project met HUD's requirements. The Authority's neighborhood stabilization manager said that the Authority's staff missed the City's buy-and-sell agreement with Properties in the City's application. A community development representative with the Authority said that since the windows of the building were boarded up, they assumed that the building was vacant and did not enter the building when they conducted a site visit. As a result, the State committed \$4.5 million in Program funds to an ineligible project.

On December 11, 2009, and as a result of our review, the Authority submitted an action plan to HUD stating it would immediately amend its grant agreement with the City of Mishawaka to remove the \$4.5 million in Program funds for the redevelopment of the Mishawaka Furniture building and in January 2010 recommend to the Authority's board the reallocation of the \$4.5

million to other projects. The action plan also stated that the Authority would review all of its Program grants with projects involving the redevelopment of demolished or vacant properties to ensure compliance with HUD’s requirements. On January 28, 2010, the Authority’s neighborhood stabilization manager stated that the Authority’s board approved the reallocation of the \$4.5 million. However, as of February 4, 2010, the Authority had not provided documentation to support that it amended its grant agreement with the City or reallocated the \$4.5 million.

RECOMMENDATIONS

We recommend that the Director of HUD’s Indianapolis Office of Community Planning and Development require the State to

- 1A. Implement its action plan by amending its grant agreement with the City of Mishawaka to remove the \$4.5 million in Program funds for the redevelopment of the Mishawaka Furniture building and award the \$4.5 million for an eligible project(s).
- 1B. Implement adequate procedures and controls to ensure that it awards Program funds for eligible projects and that its recipients use Program funds for the redevelopment of commercial buildings in accordance with HUD’s requirements.

Schedule of Funds To Be Put to Better Use 1/

<u>Recommendation number</u>	<u>Amount</u>
1A	<u>\$4,500,000</u>
Total	<u>\$4,500,000</u>

1/ 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. In this instance, if the Authority implements recommendation 1A, it will ensure that Program funds are spent according to Federal requirements.

AUDITEE COMMENTS AND OIG's EVALUATION

Ref to OIG Evaluation

Auditee Comments



February 19, 2010

Mr. Heath Wolfe
HUD Office of Inspector General for Audit
Ralph H Metcalfe Federal Building
77 West Jackson Boulevard, Suite 2646
Chicago
Illinois 60604

Dear Mr. Wolfe,

Following receipt of your draft memorandum which details your office's recent survey of our Neighborhood Stabilization Program Round 1 activities, please find below our response to your recommendations and the report in general.

During the survey completed by Office of the Inspector General (OIG) staff on IHCDA's NSP1 program the issue of ineligibility of the Mishawaka Furniture Warehouse was raised. IHCDA has duly responded to OIG's concerns and removed this property from the program as was requested. While there is still a degree of difference in the position of OIG and IHCDA regarding this property's eligibility and the auditors' interpretation of the "Vacant" definition, it has been decided not to challenge this in the interests of pragmatism to ensure that the NSP1 funding can be obligated in time. Ensuring the NSP funding is committed to the communities that we have made awards to remains our highest priority.

Since the issue with the warehouse was raised, IHCDA has implemented a clear Action Plan to address the ineligibility concerns of OIG. This approach has taken three different actions:

1. Removing the funding from the City of Mishawaka that relates to the Mishawaka Furniture Warehouse;
2. Re-writing the Vacant definition to include two separate elements - one titled Vacant (Residential) and one titled Vacant (Commercial);
3. Monitoring visits to all awardees that are using Eligible Use E to confirm property eligibility.

ADDRESS 30 South Meridian Street, Suite 1000, Indianapolis, IN 46204
PHONE 317 232 7777 TOLLFREE 800 872 0371 WEB www.ihcda.IN.gov

Comment 1
Comment 2

Ref to OIG Evaluation

Auditee Comments

Comments 1



The first two elements of this plan have been completed. The third element, the monitoring visits, have begun and are on-going. To date 11 visits have been completed, with the remaining ones scheduled to take place within the next few weeks.

IHCDA will continue to be diligent in its approach to ensure that all NSP1 funding is spent in a correct manner fulfilling the eligible uses.

Yours sincerely,

A handwritten signature in black ink that reads "Sherry Seiwert". The signature is written in a cursive, flowing style.

Sherry Seiwert
Executive Director

OIG's Evaluation of Auditee Comments

Comment 1 The Authority did not provide documentation to support that it amended its grant agreement with the City of Mishawaka to remove the \$4.5 million in Program funds for the redevelopment of the Mishawaka Furniture building.

Comment 2 HUD's frequently asked questions regarding acquisition and relocation under the Program, posted June 16, 2009, states that a vacant property is one on which the land and/or buildings are unoccupied. The Corporation was conducting its operations from the Mishawaka Furniture building as of December 2009. Therefore, the building was occupied and not vacant.