



U.S. Department of Housing and Urban Development
Region 4, Office of Inspector General
Office of Audit, Box 42
Richard B. Russell Federal Building
75 Spring Street, SW, Room 330
Atlanta, GA 30303-3388
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MEMORANDUM NO:
2011-AT-1802

January 27, 2011

MEMORANDUM FOR: José R. Rivera, Director, Community Planning and Development,
San Juan Field Office, 4ND

//signed//

FROM: James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: The Municipality of Arecibo, Arecibo, PR, Charged the HOME Program With
Expenditures That Did Not Meet Program Objectives

INTRODUCTION

We audited the Municipality of Arecibo's (Municipality) HOME Investment Partnerships Program (HOME). We selected the Municipality for review as part of our strategic plan based on the results of a previous audit of the Puerto Rico Department of Housing's (Department) HOME program, which disclosed that the Department disbursed HOME funds for land acquisition that did not meet program requirements at a 288-unit housing project named Bello Monte. During the audit, we found documentation indicating that the Bello Monte project also received HOME funds from the Municipality. The objectives of this audit were to determine whether the Municipality committed and/or disbursed HOME funds for the Bello Monte housing project and whether it met program objectives.

We provided a draft report to the Municipality on December 16, 2010, and discussed the report with Municipality officials at an exit conference on December 20, 2010. The Municipality provided written comments on January 14, 2011 and generally agreed with the recommendations. The Municipality's response, along with our evaluation of that response, can be found in appendix B of this report. Attachments to the Municipality's response were not included in the report, but are available for review upon request.

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

METHODOLOGY AND SCOPE

To accomplish our objectives, we

- Reviewed applicable statutes, regulations, and relevant HUD program requirements;
- Reviewed Municipality files associated with the Bello Monte project;
- Interviewed applicable HUD and Municipality officials;
- Reviewed all the Municipality’s HOME program obligations and disbursements associated with the Bello Monte project. Specifically, we reviewed the Municipality’s HOME program obligations and disbursements reported in HUD’s Integrated Disbursement and Information System (IDIS) for the Bello Monte project.

Our review generally covered the period July 19, 2006, through September 30, 2010. We conducted the review from October through November 2010 at the offices of the Municipal Development Department in Arecibo, PR, and the HUD Office of Community Planning and Development in San Juan, PR.

We did not conduct the audit in accordance with generally accepted government auditing standards since we did not consider the internal controls or information systems controls of the Municipality and the results of previous audits. We did not follow standards in these areas because our goal was to aid HUD in identifying potential noncompliance on the part of other participating jurisdictions that also funded the ineligible activities identified during the audit of the Puerto Rico Department of Housing. To meet our objectives, it was not necessary to fully comply with standards, nor did our approach negatively affect our review results.

BACKGROUND

The HOME program is authorized under Title II of the Cranston-Gonzalez National Affordable Housing Act as amended. HUD allocates funds by formula to eligible State and local governments for the purpose of increasing the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families. State and local governments may use HOME funds to carry out multiyear housing strategies through acquisition, rehabilitation, new housing construction, and tenant-based rental assistance. IDIS is used to monitor HOME commitments and draws for the various activities.

The Municipality has administered the HOME program since 1992. It is the eighth largest participating jurisdiction in Puerto Rico, administering more than \$2.1 million in HOME funds during the last 3 grant years as follows:

Grantee	Grant year	Authorized funds
Municipality of Arecibo	2010	\$756,658
Municipality of Arecibo	2009	759,514
Municipality of Arecibo	2008	681,771

The Municipality's Development Department was responsible for administering HOME funds. Its books and records were maintained at 158 José de Diego Avenue, Arecibo, PR.

A previous audit of the Puerto Rico Department of Housing's HOME program disclosed that HOME funds were disbursed for land acquisition that did not meet program requirements at a 288-unit housing project named Bello Monte. During the audit, we found documentation indicating that the Bello Monte project also received HOME funds from the Municipality.

The objectives of this audit were to determine whether the Municipality committed and/or disbursed HOME funds for the Bello Monte housing project and whether it met program objectives.

RESULTS OF REVIEW

The Municipality Obligated and Disbursed More Than \$115,000 in HOME Funds for Ineligible Land Acquisition at the Bello Monte Housing Project

Contrary to HUD's regulations, the Municipality disbursed HOME funds for the purchase of land that could not be used to provide housing for low- and very low-income families. Regulations at 24 CFR (Code of Federal Regulations) 92.205(a)(2) state that acquisition of vacant land must be undertaken only with respect to a particular housing project intended to provide affordable housing.

In December 2006, the Municipality disbursed \$141,000 in HOME funds to a community housing development organization (CHDO) for the acquisition of approximately 69 acres of land to develop a 288-unit housing project named Bello Monte. The land acquisition included approximately 25 acres of protected wilderness area that needed to be preserved in its natural state and could not be developed. As a result, the Municipality charged the HOME program more than \$52,000 for expenditures that did not meet program objectives and would not generate benefits or expand the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families. Therefore, the disbursement of HOME funds to acquire land not intended to provide affordable housing was not consistent with program requirements and was an ineligible use of program funds.

On July 21, 2009, the Municipality awarded the CHDO a second HOME grant totaling more than \$643,000 for the development of the Bello Monte housing project. The second grant to the CHDO included \$63,600 for the acquisition of an additional 19 acres of land that had to be preserved in its natural state for mitigation purposes.¹ Thus, the additional land could not be used to develop affordable housing for low- and very low-income families. As of November 15, 2010, no funds had been disbursed for this acquisition. The commitment of HOME funds to acquire land not intended to provide affordable housing was not consistent with program requirements. The Municipality must deobligate and reprogram the funds to other eligible efforts.

¹ The Puerto Rico Department of Natural Resources required the CHDO to transfer to the State approximately 19 acres of land to mitigate the ecological impact of the development of the Bello Monte housing project. To comply with this requirement, the CHDO planned to use HOME funds to acquire the new portion of land and transfer it to the Commonwealth of Puerto Rico.

The Bello Monte Housing Project Reflected Slow Progress

The Municipality executed an agreement in July 2006 with a CHDO for site acquisition and construction of the Bello Monte housing project. According to the agreement, the construction of the housing units should have started in July 2007, with a completion date of July 2011. However, as of November 2010, the construction had not started. Regulations at 24 CFR 92.2 state that if the project consists of rehabilitation or new construction, commitment to a specific project occurs when the participating jurisdiction and project owner have executed a written, legally binding agreement under which HOME assistance will be provided for a project of which construction can reasonably be expected to start within 12 months of the agreement date. HUD regulations at 24 CFR 92.504(a) also provide that the Municipality is responsible for managing the day-to-day operations of its HOME program, ensuring that HOME funds are used in accordance with all program requirements and written agreements, and taking appropriate action when performance problems arise. More than 4 years had elapsed, and the construction work had not started.



Although the property was acquired in August 2007, our inspection disclosed that the construction of the 288-unit housing project had not started as evidenced by these pictures.

The Municipality disbursed more than \$483,000 for the Bello Monte housing project, which reflected slow progress without assurance that the project was feasible. According to a HUD official, the project had encountered problems in complying with environmental requirements from a local agency. The Municipality failed to ensure the timely completion of the activity. As a result, HUD had no assurance that this activity provided the intended benefits and met HOME objectives.

HUD's Information System Contained Inaccurate Information

IDIS contained inaccurate information concerning the Bello Monte project. This information included incorrect funding amounts. The awarded amount shown in IDIS was incorrect, resulting in an overstatement of HOME commitments of more than \$45,000. The grant agreement amount for the Bello Monte project totaled \$1,043,035, but the funded amount according to IDIS was \$1,088,073. The Municipality's HOME program coordinator acknowledged that the HOME commitments were overstated and informed us that the Municipality would seek HUD assistance to correct the funded amount. As a result, more than \$45,000 in HOME funds was not available for use and to meet program objectives. The Municipality must deobligate and reprogram the funds to other eligible efforts.

RECOMMENDATIONS

We recommend that the Director of the San Juan Office of Community Planning and Development

- 1A. Require the Municipality to reimburse the HOME program from non-Federal funds the \$52,011 charged to its HOME program for the ineligible land acquisition.
- 1B. Determine the eligibility of the \$431,489 disbursed for the Bello Monte housing project with signs of slow progress and reevaluate the feasibility of this activity. The Municipality must reimburse HUD from non-Federal funds for any amount determined ineligible and reprogram to other eligible efforts any unexpended funds if the activity is terminated.²
- 1C. Require the Municipality to reprogram and put to better use \$63,600 in commitments for ineligible land acquisition.
- 1D. Require the Municipality to deobligate the \$45,035 in overstated HOME program commitments associated with the Bello Monte project and reprogram the funds to other eligible efforts.

² A total of \$483,500 disbursed for the Bello Monte housing project was adjusted to consider \$52,011 questioned in recommendation 1A.

Appendix A

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

<u>Recommendation number</u>	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>	<u>Funds to be put to better use 3/</u>
1A	\$52,011		
1B		\$431,489	
1C			\$63,600
1D			<u>\$45,035</u>
Total	<u>\$52,011</u>	<u>\$431,489</u>	<u>\$108,635</u>

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.

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




3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, if the Municipality implements recommendations 1C and 1D, funds improperly committed for the ineligible land acquisition and the overstated commitments will be available for other eligible activities consistent with HOME requirements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

 Escudo de Arecibo	<p>ESTADO LIBRE ASOCIADO DE PUERTO RICO GOBIERNO MUNICIPAL DE ARECIBO OFICINA DEL ALCALDE PO BOX 1086 ARECIBO, PUERTO RICO 00613</p>	<p>Tel. (787) 878-5228/879-1561 Fax (787) 880-6033</p>
<p><i>Hon. Lemuel Soto Santiago</i> <i>Alcalde</i></p>		
<p>January 13, 2011</p>		
<p>James D. McKay Regional Inspector General for Audit US Department of Housing and Urban Development Region 4, Office of Inspector General Office of Audit, Box 42 Richard B. Russell Federal Building 75 Spring Street, SW, Room 330 Atlanta, GA 30303-3388</p>		
<p>Dear Mr. McKay:</p>		
<p>Subject: Draft Audit Report 2011-AT-18XX Municipality of Arecibo HOME Program</p>		
<p>Enclosed is our response to the draft audit report on your review of the Municipality of Arecibo's HOME Investment Partnerships Program.</p>		
<p>As per your request we are providing a prompt resolution to recommendations 1A, 1C and 1D. Resolution to recommendation 1B is leave to the authority of the San Juan Field Office. The field office is aware of the development of the project and the joint effort made by the CHDO and the PJ to meet it's success. I understand that the affordable housing units presented in the project satisfy the goal of my administration to provide the low income families in Arecibo an opportunity to become homeowners.</p>		
<p>I expect the supporting documentation enclosed clear recommendations 1C and 1D and reduced the amount recommended in 1A as ineligible to the amount of \$9,442.</p>		
<p>If you have any questions in this matter, please contact the Municipal Development Director, Antonio Montalvo Jimenez at 787-878-2770.</p>		
<p>Cordially yours</p>		
 Lemuel Soto Santiago Mayor		
 <i>Un Pueblo Unido en Fe, Esperanza y Futuro</i>		

**RESPONSE TO RECOMMENDATIONS ISSUED BY THE
OFFICE OF THE INSPECTOR GENERAL ON THE
DRAFT AUDIT REPORT OF THE
MUNICIPALITY OF ARECIBO HOME PROGRAM**

- 1A. Require the Municipality to reimburse the HOME program from non-Federal funds the \$52,011 charged to its HOME program for the ineligible land acquisition.

Actions taken by the PJ.

On this recommendation we challenge that the amount disallowed is \$9,442 and not \$52,011. In order to support our allegation the following hypothesis is presented:

1. The purchase agreement executed by the Land Authority and the CHDO on August 31, 2007 established the sale price of the property in the amount \$2.5 millions. The agreement does not provide a breakdown of the appraise value by land-to-be-develop and land-to-be-preserve. Please see Exhibit I.
2. OIG established a direct participation of the municipality assuming that the amount of \$141,000 bought the whole property. The funds disbursed by the municipality provided only for the award of the option to purchase agreement and accounted only for 6% of the sale price. The option to purchase agreement was validated on December 12, 2006. Please see Exhibit II.
3. On December 10, 2010 the Land Authority issued a certification stating that the appraise value of the land-to-be-develop is \$49,000 per cuerda and the appraise value of the land-to-be-preserve is \$6,000 per cuerda. Please see Exhibit III. In addition we have requested from the Land Authority copy of the appraisal report on January 12, 2010. Please see Exhibit IV.

These facts allow us to reason the following conclusions:

1. According to the certification issued by the Land Authority, the payment distribution for the land-to-be-develop of the purchased property is \$2,343,620 for 44.88 cuerdas and \$157,380 for the land-to-be-preserve for 26.23 cuerdas. This payment distribution accounts for 94% and 6% respectively.
2. The sale price of the land-to-be-develop is \$2,342,620 and the sale price of the land-to-be-preserve is \$157,380. This distribution accounts for a 94% and 6% respectively, coincidentally the same distribution as the payment distribution mention in the item above.
3. Thus the participation of the Municipality of Arecibo in the option to purchase agreement regarding the land-to-be-preserve of the property is 6% of the \$141,000 disbursed in December 6, 2006 for \$9,442 and not \$52,010 which consider a lineal distribution on the eligibility of the land and not the eligibility of the land based by the payment made to the Land Authority.

On this train of thought 37% disallowed as the municipal share for the purchase price of the property is wrongly stated.

Comment 1

Comment 2

- 1B. Determine the eligibility of the \$431,489 disburse for the Bello Monte housing project with signs of slow progress and reevaluate the feasibility of this activity. The Municipality must reimburse HUD from non-Federal funds for any amount determined ineligible and reprogram to other eligible efforts any unexpended funds if the activity is terminated.

Actions taken by the PJ.

We understand that the decision on this recommendation has been reserve to the San Juan Field Office. We have collected several reports and documents that would be submitted to them once they decide to extend the time period for completion of this project.

This recommendation is still open.

- 1C. Require the Municipality to reprogram and put to better use \$63,600 in commitments for ineligible land acquisition.

Actions taken by the PJ.

On November 4, 2010 the CHDO submitted a request to amend the amount of \$63,000 which was originally allocated for an ineligible land acquisition. The PJ authorized the request to reprogram the funds committed increasing the funding for construction of the project.

The letter authorizing this amendment was issued in January 11, 2011 and some time next week the amendment to contract number 2010-000096 will be executed as amendment number two. This amendment will be register as contract number 2010-000096-B

Exhibits V and VI are presented as evidence of the transaction carried out. No further IDIS obligation to the CHDO project is requested.

- 1D. Require the Municipality to deobligate the \$45,035 in overstated HOME program commitments associated with the Bello Monte project and reprogram the funds to other eligible efforts.

Actions taken by the PJ.

Comment 3

Comment 4

On December 20, 2010 the HOME Program Coordinator proceed to deobligate in IDIS the amount of \$45,035 from IDIS-Activity Number 826, from the CR fund. This transaction was approved by the IDIS system the same day and could be verified by your office any time. Nevertheless, we include Exhibits VII and VIII as evidence of the transaction carried out. IDIS obligation to the CHDO project is in the amount of \$998,003.70. The remaining \$45,034.50 is allocated from the EN fund 1061 for a total of \$1,043,038.20

OIG Evaluation of Auditee Comments

Comment 1 The Municipality believes that the disallowed amount should be based on an appraised value of the land to be used for preservation purposes and that it should be required to reimburse only \$9,442.

The disallowed amount was determined based on the acquisition price of \$2.5 million for the 69 acres of land. The supporting documentation provided did not differentiate or make reference on the type(s) of property acquired or the price. The Municipality did not provide us adequate support that could substantiate their claim. Accordingly, we did not modify the report finding and recommendations.

Comment 2 The Municipality stated it will provide further information to HUD with respect to the feasibility of the Bello Monte housing project.

Comment 3 The Municipality stated it will reprogram the \$63,600 in ineligible land acquisition commitments to project construction costs. It will need to provide documentation to establish the allowability and feasibility of this action for HUD's evaluation as stated in recommendation 1B. We therefore did not modify the report finding and recommendation.

Comment 4 The Municipality stated it deobligated the \$45,035 overstated commitment. However, the Municipality did not provide us additional documentation that could demonstrate it reprogrammed the funds to other eligible efforts. It will need to provide documentation to show that the funds were properly reprogrammed.