audit report

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TO: Jorgelle Lawson, Director of Community Planning and Development, 5ED

Ronald Farrell

FROM: Ronald Farrell, Acting Regional Inspector General for Audit, 5AGA

SUBJECT: The City of Cleveland, OH, Lacked Adequate Controls Over Its HOME Investment Partnerships Program and American Dream Downpayment Initiative-Funded Afford-A-Home Program

HIGHLIGHTS

What We Audited and Why

We audited the City of Cleveland's (City) HOME Investment Partnerships Program (Program). The audit was part of the activities in our fiscal year 2010 annual audit plan. We selected the City based upon our analysis of risk factors related to Program grantees in Region V's jurisdiction, recent media coverage regarding the City's Program, and a request from the U.S. Department of Housing and Urban Development's (HUD) Columbus Office of Community Planning and Development. Our objectives were to determine whether the City complied with HUD's requirements in its use of Program and American Dream Downpayment Initiative (Initiative) funds to provide interest-free second mortgage loans to home buyers through its Afford-A-Home program and its use of recapture provisions for Afford-A-Home program activities (activity).

What We Found

The City did not comply with HUD's requirements in its use of Program and Initiative funds to provide interest-free second mortgage loans to home buyers through its Afford-A-Home program and its use of recapture provisions for activities. It (1) provided assistance for ineligible activities; (2) lacked sufficient documentation to support that activities were eligible; (3) included inappropriate recapture provisions in its action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010; (4) did not implement appropriate recapture provisions for all of the activities reviewed; and (5) did not ensure that its Program was reimbursed for Program funds used to assist home buyers in purchasing homes that were later sold through a sheriff's sale and ownership of the homes had been transferred. As a result, it inappropriately provided $20,000 in Program funds to assist two households that were not income eligible and was unable to support its use of $760,000 in Program and/or Initiative funds. Further, its Program was not reimbursed for $30,000 in Program funds used for three homes that were sold through a sheriff's sale and ownership of the homes had been transferred. In addition, the City is at risk of being required to reimburse its Program additional non-Federal funds if the ownership of additional homes acquired under its Afford-A-Home program is transferred through foreclosure.

What We Recommend

We recommend that the Director of HUD's Columbus Office of Community Planning and Development require the City to (1) reimburse its Program from non-Federal funds for the $20,000 in Program funds inappropriately used to assist two activities, (2) provide supporting documentation or reimburse its Program $760,000 from non-Federal funds, (3) reimburse its Program $30,000 from non-Federal funds for the three homes that had been sold through a sheriff's sale and ownership of the homes had been transferred, and (4) implement adequate procedures and controls to address the findings cited in this audit report. These procedures and controls should help ensure that over the next year the City appropriately recaptures Program and/or Initiative funds and/or reimburses its Program from non-Federal funds for at least $90,000 in Program and/or Initiative funds used for homes acquired under its Afford-A-Home program in which ownership would be transferred due to foreclosures.

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 and/or supporting schedules to the director of the City's Department of Community Development, the City's mayor, and/or HUD's staff during the audit. We held an exit conference with the City's director on November 18, 2010.

We asked the City's director to provide comments on our discussion draft audit report by December 3, 2010. The director provided written comments, dated

December 3, 2010. The director disagreed with our findings, but partially agreed with our recommendations. The complete text of the written comments, except for the nine appendixes of documentation that were not necessary for understanding the director's comments, along with our evaluation of that response, can be found in appendix B of this report. We provided the Director of HUD's Columbus Office of Community Planning and Development with a complete copy of the City's written comments plus the nine appendixes of documentation.

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BACKGROUND AND OBJECTIVES

The Program. Authorized under Title II of the Cranston-Gonzalez National Affordable Housing Act, as amended, the HOME Investment Partnerships Program (Program) is funded for the purpose of increasing the supply of affordable standard rental housing; improving substandard housing for existing homeowners; assisting new home buyers through acquisition, construction, and rehabilitation of housing; and providing tenant-based rental assistance. The American Dream Downpayment Assistance Act established a separate funding formula for the American Dream Downpayment Initiative (Initiative) under the Program to provide downpayment assistance, closing costs, and rehabilitation assistance to eligible first-time home buyers.

The City. Organized under the laws of the State of Ohio, the City of Cleveland (City) is governed by a mayor and a 19-member council, elected to 4-year terms. The City's Department of Community Development (Department) is responsible for planning, administering, and evaluating the City's U.S. Department of Housing and Urban Development (HUD) programs. The Department's Division of Neighborhood Services (Division) administers the City's Program- and Initiative-funded Afford-A-Home program, which helps home buyers purchase homes by offering interest-free second mortgage loans. The overall mission of the Department is to improve the quality of life in the City by strengthening neighborhoods through successful housing and commercial rehabilitation efforts, new housing construction, homeownership, and community-focused human services. The City's Program and Initiative records are located at 601 Lakeside Avenue, Cleveland, OH.

The following table shows the amount of Program and Initiative funds HUD awarded the City for fiscal years 2006 through 2010.

Fiscal year	Program funds	Initiative funds
2006	$6,323,744	$87,056
2007	6,268,729	87,056
2008	6,081,589	35,174
2009	6,763,777	
2010	6,743,584	
Totals	**$32,181,423**	**$209,286**

* Fiscal year 2008 was the last year HUD awarded Initiative funds to the City.

The City's preliminary report on the Department. On January 22, 2010, staff from the City's Office of the Mayor began a 45-day internal review of the Department's organizational structure, staff assignments, and management systems. In a memorandum, dated March 29, 2010, the chief of regional development for the City's Office of the Mayor made a preliminary recommendation for the Department to implement revised procedures and administrative reforms for its Afford-A-Home program. The new procedures included but were not limited to the establishment of (1) a loan committee responsible for reviewing and approving every property to be purchased and home buyer seeking an interest-free second mortgage loan; (2) rigorous policies related to the affordability and creditworthiness of home buyers; (3) revised mortgage, promissory note, and commitment documents; (4) standard file documentation; and (5) a rule limiting bank participation to federally regulated institutions. As of October 6, 2010, the Office of the Mayor had not finalized its internal review.

HUD's monitoring review. HUD's Columbus Office of Community Planning and Development (Office) assessed the City's Afford-A-Home program through a February 2010 monitoring review. The monitoring review covered the City's compliance with Community Development Block Grant (Block Grant) and Program requirements in the administration of its Afford-A-Home program. HUD's Office identified four findings and one concern.

Our objectives were to determine whether the City complied with HUD's requirements in its use of Program and Initiative funds to provide interest-free second mortgage loans to home buyers through its Afford-A-Home program and its use of recapture provisions for Afford-A-Home program activities (activity).

RESULTS OF AUDIT

Finding 1: The City Lacked Adequate Controls Over Its Afford-A-Home Program To Ensure That Activities Were Eligible for Assistance

The City did not comply with HUD's requirements in its use of Program and Initiative funds to provide interest-free second mortgage loans to home buyers through its Afford-A-Home program. It provided assistance for ineligible activities and lacked sufficient documentation to support that activities were eligible. These weaknesses occurred because the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements. As a result, it inappropriately provided $20,000 in Program funds to assist two households that were not income eligible and was unable to support its use of $760,000 in Program and/or Initiative funds.

The City Provided $20,000 in Program Funds for Two Ineligible Activities

We reviewed 71 of the 202 activities the City completed from January 1, 2008, through March 31, 2010. The City used $880,000 in Program and/or Initiative funds for the 71 activities.

HUD's regulations at 24 CFR (Code of Federal Regulations) 92.2 define a low-income household as a household with an annual income that does not exceed 80 percent of the median income for the area as determined by HUD. HUD's regulations at 24 CFR 92.217 state that a participating jurisdiction must invest Program funds made available during a fiscal year so that with respect to home ownership assistance, 100 percent of these funds are invested in dwelling units that are occupied by households that qualify as low-income households.

Contrary to HUD's regulations, the City drew down $20,000 in Program funds from October 14, 2008, through April 6, 2009, to assist two households that were not income eligible. The Program funds were used to provide interest-free second mortgage loans to the home buyers for activity numbers 10372 and 10793. The household income exceeded HUD's income guidelines by $9,406 (27 percent) for activity number 10793. The City could not provide sufficient income documentation for activity number 10372. However, it stated that the household was not income eligible.

The City Lacked Sufficient Documentation To Support Its Use of $760,000 in Program and/or Initiative Funds

The City lacked sufficient documentation for 60 of the 71 activities reviewed to support that it used $760,000 in Program and/or Initiative funds for eligible households and/or activities.

HUD's regulations at 24 CFR 92.203(d)(1) state that a participating jurisdiction must calculate a household's annual income by projecting the prevailing rate of the household's income at the time the participating jurisdiction determines the household to be income eligible. HUD's regulations at 24 CFR 92.251(a)(2) state that housing acquired with Program funds must meet all applicable State and local housing quality standards and code requirements. HUD's regulations at 24 CFR 92.508(a) state that a participating jurisdiction must establish and maintain sufficient records to demonstrate that each household that receives Program funds is income eligible in accordance with 24 CFR 92.203 and meets the property standards of 24 CFR 92.251. HUD's regulations at 24 CFR 92.610(c) state that the income determination requirements in 24 CFR 92.203 apply to Initiative funds. HUD's regulations at 24 CFR 92.612(b) state that housing assisted with Initiative funds must meet the property standards in 24 CFR 92.251. HUD's regulations at 24 CFR 92.616(i) state that the record-keeping requirements in 24 CFR 92.508 apply to activities assisted with Initiative funds. HUD's "Building HOME: A Program Primer," states that all housing quality standards and code requirements must be met at the time of occupancy.

Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for 58 of the 71 activities reviewed were income eligible. The City also lacked sufficient documentation to support that nine homes acquired with Program or Initiative funds met HUD's property standards requirements at the time of occupancy. The closing dates for the nine homes occurred from January 31, 2008, through April 28, 2009. The City had certificates of occupancy stating that the nine homes met the City's building and zoning codes. However, the certificates of occupancy were dated from 193 to 1,036 days (at least 6 months) before the properties were purchased by the home buyers. We did not inspect the homes since the homes were purchased nearly 1 year before the start of our audit and we would not be able to reasonably determine whether the homes met HUD's property standards requirements at the time of occupancy. The table in appendix D of this report shows the 60 activities for which the City did not have sufficient income documentation to demonstrate that households were income eligible and/or final inspection reports or certifications supporting that activities met HUD's property standards requirements at the time of occupancy.

The City did not ensure that it properly projected households' annual income for at least 65 of the 71 activities reviewed. The City used gross year-to-date income in its calculation of projected annual income rather than using current circumstances to project future income. The City also lacked documentation to support its calculation of a household's annual income or that it calculated a household's annual income for two additional activities.

HUD's February 2010 monitoring review identified that the City lacked sufficient documentation to support that households were income eligible and its calculations of households' annual income for activities. HUD requested that the City submit the required documentation and assure, in writing, that it would begin to maintain the required documentation in its activity files.

The City Lacked Adequate Procedures and Controls

The weaknesses regarding the City's providing Program and/or Initiative funds to assist a household that was overincome and lacking sufficient documentation to support that activities were appropriate occurred because the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements.

The assistant director of the City's Department stated that due to a staff error, Program funds were used to assist the household that was overincome. According to the City's Afford-A-Home policy at the time of payment, it should have assisted the household with Block Grant funds rather than Program funds. However, it would have also been contrary to HUD's regulations if the City had used Block Grant funds to provide an interest-free second mortgage loan to the home buyer for activity number 10793.

The City's internal procedures for its Afford-A-Home program only required two pay statements to be maintained for all income-producing members of a household. The commissioner of the City's Division stated that the City was not aware that HUD's requirements specified that participating jurisdictions were required to maintain 3 consecutive months' worth of income documentation on which to base a household's projected income calculation. However, the commissioner believed that the City was generally in compliance with the 3-month requirement since the majority of the activity files contained at least 3 months' worth of income documentation through a combination of year-to-date pay statement information, Internal Revenue Service form W-2 wage and tax statements, tax returns, Social Security information, and other items that were used to verify and substantiate households' income.

The assistant director of the City's Department stated that staff from the City's Division conducted closeout inspections of and completed closeout inspection forms for the homes. The purpose of the closeout inspections was to verify that all of the work in the rehabilitation specifications for the homes had been finished before the properties were purchased by the home buyers. Therefore, the staff's indication of final approval on the closeout inspection forms supported that the homes met HUD's property standards requirements at the time of occupancy. However, although the closeout inspection forms were dated within 6 months of the properties' being purchased by the home buyers, they did not state that the homes met the City's building and zoning codes. Further, the City did not have documentation to support that the homes would meet the City's building and zoning codes when all of the work described in the rehabilitation specifications was finished.

Conclusion

As previously mentioned, the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements. It inappropriately provided $20,000 in Program funds to assist two households that were not income eligible and was unable to support its use of $760,000 in Program and/or Initiative funds for the 60 activities without sufficient documentation supporting eligibility.

Recommendations

We recommend that the Director of HUD's Columbus Office of Community Planning and Development require the City to

1A. Reimburse its Program from non-Federal funds for the $20,000 in Program funds inappropriately used to assist activity numbers 10372 and 10793.

1B. Provide supporting documentation or reimburse its Program from non-Federal funds, as appropriate, for the $760,000 in Program and/or Initiative funds used for the 60 households and/or activities for which the City did not have sufficient income documentation to demonstrate that households were income eligible and/or final inspection reports or certifications supporting that activities met HUD's property standards requirements at the time of occupancy.

1C. Implement adequate procedures and controls to ensure that Program and Initiative funds are only used for eligible households and that it maintains documentation to sufficiently support the eligibility of households and activities in accordance with HUD's requirements.

1D. Review the remaining 131 (202 minus 71) activities to determine whether the households were income eligible and/or homes met HUD's property standards requirements at the time of occupancy. For the activities that received improper assistance, the City should reimburse its Program the applicable amount from non-Federal funds.

Finding 2: The City Lacked Adequate Controls Over Its Afford-A-Home Program To Ensure That Appropriate Recapture Provisions Were Used for Activities

The City did not comply with HUD's requirements in its use of recapture provisions for activities. It (1) included inappropriate recapture provisions in its action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010; (2) did not implement appropriate recapture provisions for all 71 of the activities reviewed; and (3) did not ensure that its Program was reimbursed for Program funds used to assist home buyers in purchasing homes that were later sold through a sheriff's sale and ownership of the homes had been transferred. These weaknesses occurred because the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements. As a result, its Program was not reimbursed for $30,000 in Program funds used for three homes that were sold through a sheriff's sale and ownership of the homes had been transferred. Further, the City is at risk of being required to reimburse its Program additional non-Federal funds if the ownership of additional homes acquired under its Afford-A-Home program is transferred through foreclosure. Based on our sample, we estimate that over the next year, the City will not recapture Program and/or Initiative funds and/or reimburse its Program from non-Federal funds for at least $90,000 in Program and/or Initiative funds used for homes acquired under its Afford-A-Home program in which ownership would be transferred due to foreclosures.

The City Did Not Include Appropriate Recapture Provisions in Its Action Plans

HUD's regulations at 24 CFR 91.220 state that if a participating jurisdiction intends to use Program funds for home buyers, it must state the guidelines for resale or recapture, as required in 24 CFR 92.254, in its action plan. HUD's regulations at 24 CFR 92.254(a)(4) state that Program-assisted housing must meet HUD's affordability requirements. Section 92.254(a)(5) states that to ensure affordability, a participating jurisdiction must impose either resale or recapture provisions that comply with the standards of section 92.254(a)(5) and include those provisions in its consolidated plan. Section 92.254(a)(5)(ii) states that in establishing its recapture provisions, the participating jurisdiction is subject to the limitation that when the recapture provision is triggered by a voluntary or involuntary sale of the housing unit and there are no net proceeds or the net proceeds are insufficient to repay the Program investment due, the participating jurisdiction can only recapture the net proceeds, if any. The recaptured funds must be used to carry out Program-eligible activities in accordance with the requirements of 24 CFR Part 92. HUD's regulations at 24 CFR 92.502(c)(3) state that a participating jurisdiction must disburse Program funds, including recaptured Program funds, in its HOME investment trust fund local account (local account) before requesting Program funds from its HOME investment trust fund treasury account (treasury account).

The City did not ensure that it included appropriate recapture provisions in its action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010. The action plans stated that if the owner resold the property or ceased to use it as a primary residence during the Program compliance period, the amount of the loan would be due and payable in full. If a property went into foreclosure, the recapture amount would be the net proceeds from the foreclosure sale in an amount not to exceed the original Program investment. However, the City did not limit the amount of Program funds that could be recaptured from a nonforeclosure sale to the net proceeds from the sale of the property. The City also included recapture provisions in its action plans which inappropriately stated that Program funds recaptured would be used to make additional loans to low-income home buyers.

The City Did Not Implement Appropriate Recapture Provisions for Its Activities and Did Not Reimburse Its Program $30,000 From Non-Federal Funds

We statistically selected 71 of the 202 Program- and/or Initiative-funded activities the City completed from January 1, 2008, through March 31, 2010. The 71 activities totaled $880,000 in Program and/or Initiative funds.

HUD's regulations at 24 CFR 92.612(c) state that housing assisted with Initiative funds must meet the affordability requirements in 24 CFR 92.254(a). HUD's HOMEfires, volume 5, number 2, states that for Program-assisted home-buyer projects with recapture provisions, the amount of Program funds required to be repaid in the event of foreclosure is the amount that would be subject to recapture under the terms of the written agreement with the home buyer. If the recapture provisions require the entire amount of the Program investment from the home buyer or an amount reduced prorata based on the time the home buyer has owned and occupied the home measured against the affordability period, the amount required by the recapture provisions is the amount that must be recaptured by the participating jurisdiction for the Program. If the participating jurisdiction is unable to recapture the funds from the household, it must reimburse its Program in the amount due pursuant to the recapture provisions in the written agreement with the home buyer.

Contrary to HUD's requirements, the City did not ensure that it implemented appropriate recapture provisions for all 71 of the activities reviewed. Although the mortgages and promissory notes between the City and the home buyers included affordability requirements, neither the mortgages nor the promissory notes contained language that limited the amount of Program and/or Initiative funds the City could recapture to the net proceeds from the sale of a home. The mortgages and promissory notes required repayment of the full amount of the loan upon sale, lease, refinance, or transfer. An additional amount equal to the interest which would have accrued on the second mortgage loan if it had been made at the same interest rate as the first mortgage loan was also due and payable in the event that the borrower sold, leased, refinanced, or transferred the property within the initial 5 years of the execution of the mortgage and promissory note.

As previously stated, the mortgages and promissory notes required repayment of the entire amount of the Program investment upon sale. As of September 30, 2010, the City received foreclosure notices for the homes of 31 of the 202 activities completed from January 1, 2008, through March 31, 2010. Therefore, we reviewed the 31 activities to determine whether the homes had been sold and ownership of the homes had been transferred. Three of the homes had been sold through a sheriff's sale, and ownership of the homes had been transferred as of October 29, 2010. The City did not receive any net proceeds from the sale of the three homes or reimburse its Program for the $30,000 in Program funds used for the three homes. The following table includes the activity number, the date of closing, the date Program funds were drawn down for the activity in HUD's Integrated Disbursement and Information System (System), the date the home was sold through a sheriff's sale, the date ownership was transferred, and the amount of assistance provided for the three homes.

Activity number	Date of closing	Date of drawdown	Date of sheriff's sale	Date of ownership transfer	Amount of assistance
10093	Feb. 8, 2008	Feb. 29, 2008	Aug. 24, 2009	Oct. 8, 2009	$10,000
10368	Aug. 28, 2008	Oct. 14, 2008	Sept. 21, 2009	Dec. 4, 2009	10,000
10396	Oct. 2, 2008	Oct. 14, 2008	Apr. 12, 2010	Oct. 15, 2010	10,000
Total					$30,000

HUD's February 2010 monitoring review identified that the City's mortgages and promissory notes with home buyers did not include language that limited the amount of Program funds the City could recapture to the net proceeds from the sale of a home and indicated that the City was not receiving any net proceeds from the sale of homes or reimbursing its Program from non-Federal funds for the Program funds used for homes that were sold through a sheriff's sale. HUD requested that the City determine the number of homes that had been sold through a sheriff's sale as of January 1, 2007, and reimburse its Program from non-Federal funds for the Program funds used for the homes.

The City Lacked Adequate Procedures and Controls

The weaknesses regarding the City (including (1) inappropriate recapture provisions in its action plans, (2) not implementing appropriate recapture provisions for its activities, and (3) not ensuring that its Program was reimbursed for Program funds used to assist home buyers in purchasing homes that were later sold through a sheriff's sale and ownership of the homes had been transferred) occurred because the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements.

The assistant director of the City's Department stated that until HUD's February 2010 monitoring review, the City was not aware that it was required to include language in its mortgages and promissory notes that limited recapture to the net proceeds from the sale of homes and by excluding such language, it created a potential financial burden on itself. Further, the assistant director stated that although the City was not aware that it had created the additional financial burden on itself, it complied with HUD's requirements and State law regarding foreclosure sales and did not recapture more than the net proceeds from the sale of homes.

The City included appropriate recapture provisions in its action plan for program years 2010 to 2011. In addition, it developed a revised mortgage and promissory note for its activities and began using them on April 9, 2010. The revised mortgage and promissory note included appropriate recapture provisions. Specifically, the documents contained language that limited the amount of Program and/or Initiative funds the City could recapture to the net proceeds from the sale of a home.

Conclusion

As previously mentioned, the City lacked adequate procedures and controls regarding its Afford-A-Home program to ensure that it appropriately followed HUD's requirements. It (1) included inappropriate recapture provisions in its action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010; (2) did not implement appropriate recapture provisions for all 71 of the activities reviewed; and (3) did not ensure that its Program was reimbursed for the $30,000 in Program funds used for the three homes that were later sold through a sheriff's sale and ownership of the homes had been transferred. Further, the City is at risk of being required to reimburse its Program additional non-Federal funds if the ownership of additional homes acquired under its Afford-A-Home program is transferred through foreclosure. If the City implements adequate procedures and controls over its Afford-A-Home program to ensure compliance with HUD's requirements regarding homes acquired under the Afford-A-Home program in which ownership is transferred due to foreclosures, we estimate that over the next year, the City will appropriately recapture Program and/or Initiative funds and/or reimburse its Program from non-Federal funds totaling at least $90,000. Our methodology for this estimate is explained in the Scope and Methodology section of this audit report.

Recommendations

We recommend that the Director of HUD's Columbus Office of Community Planning and Development require the City to

2A. Reimburse its Program $30,000 from non-Federal funds for the three homes that had been sold through a sheriff's sale and ownership of the homes had been transferred.

2B. Implement adequate procedures and controls to ensure that if the ownership of additional homes acquired under its Afford-A-Home program is transferred through foreclosures, the City recaptures the entire amount of the Program and/or Initiative funds through the receipt of net proceeds from the sales of the homes and/or reimburses its Program from non-Federal funds for the Program and/or Initiative funds provided to the home buyers, as appropriate. This will ensure that over the next 12 months the City appropriately recaptures Program and/or Initiative funds and/or reimburses its Program from non-Federal funds totaling at least $90,000.

SCOPE AND METHODOLOGY

To accomplish our objectives, we reviewed

- Applicable laws; HUD's regulations at 24 CFR Parts 35 and 92; HUD's "Building HOME: A Program Primer"; HUD's HOMEfires, volume 5, numbers 2 and 5; HUD's Technical Guide for Determining Income and Allowances for the Program; and HUD's guidebook "Fitting the Pieces Together."

- The City's accounting records; audited financial statements and single audit reports for the years ending December 31, 2006, 2007, and 2008; data from HUD's System; Program and Initiative activity files; policies and procedures; organizational chart; consolidated plan for 2005 through 2010; action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010; and consolidated annual performance and evaluation reports for program years 2007 and 2008.

- HUD's files for the City.

In addition, we interviewed the City's employees, Program participants, and HUD's staff.

Finding 1

We statistically selected 71 of the 202 Program- and/or Initiative-funded activities the City completed from January 1, 2008, through March 31, 2010, to determine whether the City used Program and Initiative funds for eligible activities. The 71 activities totaled $880,000 in Program and/or Initiative funds. Our sampling criteria used a 90 percent confidence level, 20 percent error rate, and precision of plus or minus 10 percent.

Finding 2

We statistically selected 71 of the 202 Program and/or Initiative-funded activities the City completed from January 1, 2008, through March 31, 2010, to determine whether the City implemented appropriate recapture provisions for its activities. The 71 activities totaled $880,000 in Program and/or Initiative funds. Our sampling criteria used a 90 percent confidence level, 20 percent error rate, and precision of plus or minus 10 percent. As previously stated, the mortgages and promissory notes required repayment of the entire amount of the Program investment upon sale. As of September 30, 2010, the City received foreclosure notices for the homes of 31 of the 202 activities completed from January 1, 2008, through March 31, 2010. Therefore, we reviewed the 31 activities to determine whether the homes had been sold and ownership of the homes had been transferred. Three of the homes had been sold through a sheriff's sale and ownership of the homes had been transferred as of October 29, 2010. The City did not receive any net proceeds from the sale of the three homes or reimburse its Program for the $30,000 in Program funds used for the three homes. Further, the homes for two of the activities were no longer in foreclosure as of October 29, 2010. In addition, four of the homes involved conventional mortgages that were not Federal Housing Administration (FHA)-insured.

To estimate the number of homes in foreclosures that would result in a sale and transfer of ownership within the next year, we modeled the rates of conversion for homes in foreclosure to sale and transfer of ownership within the state of Ohio. Loans for the homes in foreclosure were grouped and modeled by the year of origination as the year of origination has been shown to affect the length of time in foreclosure before a resale and transfer of ownership. Sale and transfer of ownership patterns for homes in foreclosure from 2008 were used to model 2009 loans for the homes in foreclosure as these two years showed the same probability distribution and the data for 2008 was more complete. To model the rates of conversion to sale and transfer of ownership, we used histories from 1,422 foreclosed Ohio loans from HUD's FHA databases to create a declining probability distribution (i.e. a survival curve) for the state of Ohio. This curve modeled the percentage of homes in foreclosure (S) which remained unsold at a given number of months after going into foreclosure. Using this information, we estimated for each of the City's 22 homes with FHA-insured mortgages in foreclosure as of October 29, 2010, a home's likelihood of surviving foreclosure to a certain point in time without going to sale and transfer of ownership. The probability of going to sale and transfer of ownership was then summed for the 22 homes to estimate the total number of homes in foreclosure that would be sold and transferred to new owners within the next year. To estimate the probability that an individual home would go to sale and ownership would be transferred, the survival at the time of observation (S_{curr}) was compared with the survival probability one year from October 29, 2010 (S_{futr}), and the likelihood of sale and transfer of ownership ($\mathrm{P}_{\mathrm{sale}}$) was computed as follows:

$$\mathrm{P}_{\mathrm{sale}} = (1 - \frac{\mathrm{S}_{\mathrm{futr}}}{\mathrm{S}_{\mathrm{curr}}})$$

Based on our modeling, we estimated that at least nine of the City's 22 homes with FHA-insured mortgages in foreclosure as of October 29, 2010, would be sold and ownership would be transferred within the next year. Making the conservative assumption that each loan would involve at least $10,000 in Program and/or American Dream Downpayment Initiative (Initiative) funds, we estimated that over the next year, the City will not recapture Program and/or Initiative funds and/or reimburse its Program from non-Federal funds for at least $90,000 in Program and/or Initiative funds used for at least nine homes acquired under its Afford-A-Home program in which ownership would be transferred due to foreclosures. This estimate is presented solely to demonstrate the amount of Program and/or Initiative funds that could be put to better use over the next year on eligible activities if the City implements our recommendation.

In addition, we relied in part on data maintained by the City for its Afford-A-Home program, data in HUD's System, and selected data from HUD's Single Family Data Warehouse. Although we did not perform detailed assessments of the reliability of the data, we performed minimal levels of testing and found the data to be adequately reliable for our purposes.

We performed our onsite audit work from April through August 2010 at the City's offices located at 601 Lakeside Avenue, Cleveland, OH. The audit covered the period January 2008 through March 2010 and was expanded as determined necessary.

We performed 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 a process adopted by those charged with governance and management, designed to provide reasonable assurance about achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objectives:

- Effectiveness and efficiency of operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

- Reliability of financial reporting – 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 deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness and efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws or regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- The City lacked adequate procedures and controls to ensure that (1) it used Program and/or Initiative funds for activities in accordance with HUD's requirements; (2) it included appropriate recapture provisions in its action plans for program years 2007 to 2008, 2008 to 2009, and 2009 to 2010; (3) it implemented appropriate recapture provisions for activities; and (4) its Program was reimbursed for Program funds used to assist home buyers in purchasing homes that were later sold through a sheriff's sale and ownership of the homes had been transferred (see findings 1 and 2).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1A	$20,000		
1B		$760,000	
2A	30,000		
2B			$90,000
Totals	$50,000	$760,000	$90,000

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 polices 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. This includes reduction in outlays, deobligation of funds, withdrawal of interest subsidy 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 City implements our recommendation it will appropriately recapture Program and/or Initiative funds and/or reimburse its Program from non-Federal funds.

Appendix B

AUDITEE COMMENTS AND OIG's EVALUATION

Ref to OIG Evaluation **Auditee Comments**

City of Cleveland
Frank Jackson, Mayor

Department of Community Development
Directors Office
601 Lakeside Avenue, Room 320
Cleveland, Ohio 44114-1070
216-664-4000
www.city.cleveland.oh.us

December 3, 2010

Mr. Heath Wolfe
Regional Inspector General for Audit
Office of Inspector General, U.S. Department of Housing and Urban Development
77 W. Jackson Blvd., Room 2646
Chicago, Il 60604

Re: Discussion Draft of the Audit Report City of Cleveland HOME Investment Partnership Program Dated 11/10/2010

Dear Mr. Wolfe:

This letter is in response to the Audit Discussion Draft issued by your office on November 10, 2010.

During this audit, our staff provided your office with 202 records related to the HOME Investment Partnership Program covering the period from January 1, 2008 to March 31, 2010. Your staff selected 71 files for detailed review.

Your review generated two (2) draft findings regarding the City's administration of the HOME Investment Partnership Program. Enclosed with this letter is the City of Cleveland's Management Response to the draft findings. We will also provide a CD ROM of the appendices referenced. The appendices are provided for your review. They are not intended to be published as part of our response.

While the City has reservations regarding the specifics of the findings and believes that it has met both the spirit and the letter of HUD regulations in its administration of the Afford-A-Home program, I would like to express my appreciation to you and your staff for your thorough review. If you have any questions or require further information please feel free to contact me at (216) 664-4288.

Respectfully Submitted,

Daryl P. Rush, Director
Department of Community Development

Ref to OIG Evaluation	Auditee Comments

City Of Cleveland Management Response to OIG Discussion Draft Delivered 12/3/2010

The discussion draft audit of the City of Cleveland HOME Investment Partnership Program (Afford-A-Home) sent on November 10, 2010 generated two (2) findings and made recommendations with respect to each of those findings. Below is the management's response to each finding and recommendation.

Finding 1: The City lacked adequate controls over its Afford-A-Home Program to ensure activities were eligible for Assistance and, for nine (9) activities, the City provided insufficient evidence that property standards were met at the time of occupancy.

Comments 1 and 2

Management Response – Disagree: HUD allows local governments to develop their own income verification procedures. The City's procedures were found to be sufficient by HUD in the past.

Comment 3

In the only activity cited by the Office of Inspector General (OIG) as being over the income limits, the City was in the process of using non-HOME funds to meet its obligation to the homebuyer at the time of the auditor's review. This process of using non-HOME funds for this case has been completed. In the other 66 activities cited for issues related to income verification methods, the City re-examined the files to confirm income eligibility.

Detailed schedules relating to the City's re-examination are included in the City's responses to Recommendation 1B herein. In summary, the City found:

Comment 4

1. For one (1) activity, the family had a fixed income from public assistance sources and the benefit information in the files is sufficient to make an affirmative eligibility determination.

Comment 1

2. For thirty-eight (38) activities, the City used its longstanding practice of requiring two (2) pay stubs plus W2s[1] or the IRS Form 1040 (1040) for the previous year. HUD found this documentation to be acceptable for HOME funds in its monitoring visits conducted in 2006, 2007, and 2008. Nonetheless, the Draft Discussion report cites three (3) consecutive months of income documentation in the Technical Guide for Determining Income

[1] City income tax in the State of Ohio is imposed on ***all*** salaries, wages, commissions, other income, and other compensation earned and received. The income information on the W2 must include city income to be acceptable.

Ref to OIG Evaluation	**Auditee Comments**
Comment 5 Comments 4, 5, and 6	and Allowances for the HOME Program. In these thirty-eight (38) activities the Year-To-Date (YTD) information shown on pay stubs in the file meets or exceeds this guideline. This YTD documentation shows that all thirty-eight (38) households had incomes meeting HOME eligibility requirements.
Comments 5 and 7	3. For eight (8) activities, the file contained only one (1) pay stub with YTD information going back three (3) or more months. This YTD documentation meets or exceeds the guideline and shows that all eight (8) households had incomes meeting HOME eligibility requirements.
Comments 5 and 8	4. For four (4) activities, the file contains at least one (1) pay stub issued during the first quarter of the calendar year. YTD information shown on these pay stubs in addition to the previous year W2s provide documentation of income going back three (3) or more months. This documentation meets or exceeds the guideline and shows that all four (4) households had incomes meeting HOME eligibility requirements.
Comments 5, 9 and 10	5. For two (2) activities the applicants were seasonal workers and a twelve (12) month income review was completed of current pay stubs, the previous year's W2s, and the previous year's IRS Form 1040 (1040). This documentation meets or exceeds the guideline and shows that both households had incomes meeting HOME eligibility requirements.
Comment 1	6. For twelve (12) activities, the City's original income determination was based on the method found appropriate by previous HUD monitoring guidance – namely utilizing two (2) pay stubs, previous year W2 information, and previous year 1040 information. Additional information will be required to meet the HUD auditor's request that we gather three consecutive months of income documentation. The City is committed to seeking this additional information in order to complete its reexamination of these twelve (12) activities.
Comments 11	7. For one (1) activity, the City's re-examination shows a household to have been over-income at the point of application. The City miscalculated the household's projected annual income. As a result, the City will remove this activity from IDIS and will meet its commitment to the homebuyer from non-federal sources.

Ref to OIG Evaluation	Auditee Comments

Recommendation 1A: Reimburse its Program from non-federal funds for the $10,000 in Program funds used to assist activity number 10793.

Comment 3

Management Response –Agree: The City acknowledges that assistance was provided to an ineligible buyer for activity 10793 and has removed this activity from its IDIS reporting system and has met its second mortgage commitment to the buyer using non-federal funds.

Recommendation 1B: Provide supporting documentation or reimburse its Program from non-federal funds, as appropriate, for (1) the sixty-six (66) households for which the City did not have three months of pay stubs and (2) the nine (9) activities where the documentation of the final inspection conducted within six (6) months of occupancy did not certify that the home inspected met local code requirements.

Comment 12

Management Response to 1B(1) – Disagree - The City collected information sufficient to verify and project income, and provided assistance to qualified families.

Comment 12

Comment 13

Before providing a detailed case-by-case response, the City contends it has abided by HUD's guidelines found within chapter 2 of HUD's Technical Guide for Determining Income and Allowances for the HOME Program. The applicable guideline reads:

PJs may develop their own verification procedures provided they collect source documentation and that this documentation is sufficient for HUD to monitor program compliance.

Comment 13

Comments 1 and 2

Accordingly, the City had a procedure requiring the submission of two (2) pay stubs, previous year W2s, and previous year 1040 documents by the applicants. By reviewing YTD information on the pay stubs and/or the W2 or 1040 documents (especially important for income calculations conducted during the first quarter of a calendar year) the City procedure was designed to capture information documenting at least three consecutive months worth of income information. This procedure, in fact, has been accepted by the HUD Columbus Office during monitoring reviews of Cleveland's HOME program.

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Ref to OIG Evaluation	**Auditee Comments**

The City has re-examined income documents on all sixty-six (66) activities cited by HUD. Consistent with the summary provided above in the response to Finding #1, the following is a detailed case-by-case response:

1. Benefits Based Determination – 1 Activity

Comment 4

The City requires third party verification for non-employment related income such as SSI, child support or other benefits. Schedule 1 lists one (1) activity where the primary income source was from a benefits program and income could be projected accordingly. Appendix A contains the background material and income projections for this case. **The buyer listed in Schedule 1 is clearly income eligible as originally determined by City staff.**

Schedule 1: Benefits Based Determination

	IDIS	Estimated Income	Qualifying Income
1	10458	21,352	34,800

2. Income Documentation With At Least Three (3) Consecutive Months In YTD Income Provided With Available Information – Thirty-Eight 38 Activities

Comment 5

In the period January 1, 2008 through October 1, 2010, the City required that employment income documentation include at least two (2) pay stubs and income tax information from two (2) previous years when assessing employment based income. In light of the auditor's comment, Schedule 2 lists 38 activities where the YTD information on one or more of the pay stubs in the file covers three or more consecutive months of earned income. The documentation gathered meets or exceeds the guideline. Appendix B contains the YTD income documentation for each of these activities. City staff has re-examined its income projections for each of these activities. **All the buyers in Schedule 2 are income eligible as originally determined by City staff**.

Comments 4, 5, and 6

Ref to OIG Evaluation **Auditee Comments**

Comments 4, 5, and 6

Schedule 2: Three (3) Months Of Income In YTD Statement
From Two (2) Pay Stubs

	IDIS	Estimated Income	Qualifying Income
1	9852	47,620	48,150
2	10075	31,041	39,300
3	10093	39,542	44,200
4	10096	37,294	39,300
5	10163	24,691	39,300
6	10171	32,555	39,750
7	10173	37,353	49,100
8	10174	31,928	34,350
9	10176	29,702	39,750
10	10229	39,210	49,700
11	10232	41,977	53,700
12	10299	28,497	44,750
13	10301	22,712	44,750
14	10359	27,040	49,700
15	10360	38,750	39,300
16	10361	25,303	39,750
17	10367	18,997	39,750
18	10396	25,041	44,750
19	10457	17,808	39,300
20	10631	33,781	44,750
21	10686	29,702	39,750
22	10690	40,064	44,750
23	10691	39,478	39,750
24	10769	24,684	34,800
25	10773	29,120	44,750
26	10794	36,426	39,750
27	10796	32,388	34,800
28	10866	31,230	41,500
29	10867	21,209	44,750
30	10868	38,832	41,500
31	10888	31,701	41,500
32	10911	37,917	46,650
33	10961	29,486	36,300
34	10964	40,403	41,500
35	10994	31,492	36,300
36	11073	27,840	36,300
37	11082	42,907	46,650
38	11087	35,171	41,500

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Ref to OIG Evaluation — Auditee Comments

3. YTD Information Available With One (1) Pay Stub And YTD Information Covering At Least Three (3) Consecutive Months – Eight (8) Activities

Comments 5 and 7

Schedule 3 lists activities where a single pay stub is available in our records, but the YTD information on that pay stub covers more than three months of earnings and provides the information needed to document consistent earnings for the purposes of projecting eligibility. The documentation gathered meets or exceeds the guideline. Appendix C contains the information and income projections. City staff has re-examined its income projections for each of these activities. **All the buyers in Schedule 3 are clearly income eligible as originally determined by City staff**.

Schedule 3: YTD Of At Least Three (3) Months From One Available Pay Stub

	IDIS	Estimated Income	Qualifying Income
1	10079	43,907	49,100
2	10368	31,076	34,800
3	10455	21,612	44,750
4	10797	30,250	39,750
5	10802	31,761	39,750
6	10818	25,486	44,750
7	10824	48,270	49,700
8	10865	36,005	41,500

4. YTD Information Available With Pay Stub From 1st Quarter And W2(S) From The Previous Year – Four (4) Activities

Comments 5 and 8

Schedule 4 lists activities where two or more pay stubs issued in the 1st quarter of the year are available in our records. These pay stubs are supplemented with the W2s from the previous year to provide at least three consecutive months of income documentation. These records provide the information needed to document consistent earnings. The documentation gathered meets or exceeds the guideline. Appendix D contains the pay stubs, W2s, and income projections. City staff has re-examined its income projections for each of these activities. **All the buyers in Schedule 4 are clearly income eligible as originally determined by City staff**.

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Comments 5 and 8

Schedule 4: First Quarter Pay Stub With YTD, Plus Previous W2(S)

	IDIS	Estimated Income	Qualifying Income
1	10162	28,184	34,800
2	10870	29,120	39,750
3	10821	44,751	49,700
4	10846	45,803	56,000

5. Seasonal Employment Twelve (12) Month Review – Two (2) Activities

Comments 5, 9, and 10

Schedule 5 lists activities where workers are seasonal and a twelve month income review is appropriate. The files contain at least 2 pay stubs and W2 or 1040 information as appropriate. The documentation gathered meets or exceeds the guideline. Appendix E contains the information and income projections. City staff has double checked its income projections for each of these activities. **All the buyers in Schedule 5 are clearly income eligible as originally determined by City staff**.

Schedule 5: Seasonal Workers – Twelve (12) Month Income Review

	IDIS	Estimated Income	Qualifying Income
1	10161	23,521	34,800
2	10157	39,948	49,100

For these reasons the City believes the OIG should not mandate repayment for the activities listed in Schedules 1 through 5 above.

6. Files For Follow-Up Or Other Concerns – Twelve (12) Activities

Finally, The City proposes follow-up with developers, buyers, and buyer's employers for the activities identified in Schedule 6 to collect additional earnings information where the pay stubs, W2s and 1040 information in the files do not provide three months of *consecutive* income documentation. Based upon the auditor's finding we are seeking supplemental information that would

Ref to OIG Evaluation	Auditee Comments

show consistency of earnings for the 3 month period leading up to application. This action will require the cooperation of multiple parties and the City requests that it have sufficient time to provide information for the activities identified in Schedule 6. To the extent that this review and supplemental information confirms buyer eligibility shown on the schedule, we ask that these activities be deleted from the Finding. In the event that the supplemental information shows that buyers were not eligible for assistance, the City will reimburse the HOME account from non-federal funds.

Comment 14

Schedule 6: City To Seek Additional Information

	IDIS
1	10109
2	10169
3	10289
4	10291
5	10362
6	10420
7	10634
8	10638
9	10771
10	10772
11	10991
12	10992

7. Found To Be Over-Income During Re-Examination – One (1) Activity

Comment 11

Finally, the City has identified one (1) activity, specifically activity 10372, where the re-examined projected income was greater than HOME requirements. The original determination by city staff was based upon a faulty income projection. This activity will be removed from IDIS and the City will meet its second mortgage commitment to this buyer with non-federal funds.

Conclusion

Although the City has collected three consecutive months of income documentation, HUD regulations at 24 CFR 92.203(a)(2) state that a participating jurisdiction must determine household's annual income by examining source documentation evidencing

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Ref to OIG Evaluation **Auditee Comments**

households' annual income. The regulations do not mandate any particular number of pay stubs or other specific documentation for use in determining the income.

Comment 13

Chapter two of HUD's Technical Guide for Determining Income and Allowances for the HOME Program, dated January 2005, (Guide) states that a participating jurisdiction may develop its own income verification procedures. The Guide does not require any particular number of pay stubs or otherwise specifically require any particular document be used. Where income is deemed to be stable, it is suggested that three (3) month's of income documentation is an appropriate amount upon which to base a household's projected income calculation for the following twelve month period. "Income documentation" is not defined and the Guide does not state that three month's of pay stubs is required. In fact, the example given in the Determining Income and Allowances Training Manual, dated May 2007, (Manual) uses only three (3) pay stubs covering six consecutive weeks and showing YTD income information to calculate the income projection (please see the exercise from the Manual attached in Appendix F). The City required that applicants provide at least 2 pay stubs, the prior year's tax return, and prior year's W2(s). By using pay stubs, the YTD payment information on the pay stubs, the prior year's tax return and prior year's W2(s), the City was able to meet or exceed the three months of income documentation suggested.

Comments 5 and 9

The HUD Columbus office has completed yearly monitoring reviews of the City's various HUD funded programs. In particular, 2006, 2007, and 2008, reviews were completed for the HOME Program income eligibility. The monitoring reports indicated there was no issue with the method the City used to calculate income eligibility. Until the February, 2010 site visit, from the HUD Columbus Office, the City had no additional communication with the HUD Columbus Office to indicate there was a change in the procedure of how income eligibility must be calculated. The City has taken action since the February site visit follow-up letter and the OIG review to conform to the new requirements. Given these conditions the City should not be penalized for using calculations that were previously approved by the HUD Columbus Office to determine income eligibility.

Comment 1

Ref to OIG Evaluation	Auditee Comments
Comment 15 Comment 15 Comment 16	**Management Response to 1B(2) – Disagree: The City inspected the properties within six (6) months of closing by qualified staff.** The City's Afford-A-Home policy calls for multiple checks and balances regarding the physical standards required for a structure to qualify for assistance. The first is that developers provide specifications that show the house will meet or exceed local code standards upon completion. Second, the developer of each Afford-A-Home house must pull permits from the Department of Building and Housing and those permits are closed only when the work performed meets the relevant code. The developer must also secure a Certificate of Occupancy. The Certificate of Occupancy is issued at the time that construction is complete and contains evidence of code compliance for all systems in the house. Once a Certificate of Occupancy is issued it remains in force unless the property's use is changed or the property is condemned. Third, when a buyer elects to purchase a house using Afford-A-Home Assistance whether shortly after issuance of the Certificate of Occupancy or at a later date, the project is re-inspected by a trained, certified Rehabilitation Inspector to verify that the house is in the same condition that it was in when the Certificate of Occupancy was issued and the work identified in the specifications was completed. The evidence of this inspection is the final inspection form. In the event that the property needs additional work before it meets the appropriate standards, then the Rehabilitation Inspector creates a punch list. The house is re-inspected after the punch list items are completed and the final inspection form is completed. Appendix G includes a copy of the final inspection form, the punch list form, and the relevant pages from the City of Cleveland Department of Community Development General Specification Manual last updated on March 6, 2006.
Comment 17	The City's Rehabilitation Inspectors are trained in assessing compliance with the General Specification Manual. That manual requires that the specifications for work conducted on a house assisted with HOME funds must cover all items needed for the house to meet local codes. Further, the Rehabilitation Inspectors all are certified as Residential Building Inspectors, a certification of the State of Ohio.
Comment 18	**For eight (8) activities cited by the auditor and listed on Schedule 7, the final inspection occurred within six months of occupancy by the assisted buyer.** This is noted in the file as approval of a "final inspection."
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Ref to OIG Evaluation

Auditee Comments

Comment 18

Schedule 7: Inspection and Closing Dates for eight (8) activities

	IDIS	Final Inspection Date	Closing Date
1	10162	3/27/2008	4/22/2008
2	10173	1/18/2008	1/31/2008
3	10174	4/23/2008	4/18/2008
4	10232	5/1/2008	5/30/2008
5	10420	7/31/2008	7/31/2008
6	10457	10/10/2008	10/17/2008
7	10458	9/19/2008	12/13/2008
8	10638	11/14/2008	12/10/2008

For this reason, HUD should not require repayment of funds related to the eight (8) projects identified as failing to have sufficient documentation of physical condition at time of purchase.

Information in the file for activity 10867 shows that additional non-code work was needed to complete the work specified. The City needs to review additional documents to provide evidence that the specified work was completed before occupancy.

Comment 19

Having received notice through the discussion draft that the final inspection document should include specific language related to code compliance on its final inspection form, the City has adopted the final inspection form in Appendix H.

Ref to OIG Evaluation	Auditee Comments

Recommendation 1C: Implement adequate procedures to sufficiently support income eligibility.

Comment 20

Management Response – Agree: The City has implemented new controls regarding the approval of Afford-A-Home (AAH) projects. Beginning in December of 2009, all AAH applications were reviewed by a committee consisting of the Chief of Regional Development, the Director of Community Development, the Assistant Director of Community Development, and the Commissioner of the Division of Neighborhood Services. In addition to reviewing all new AAH activities, this committee also developed and adopted new rules with respect to underwriting and down payments in the AAH Program. The purpose of these standards was to ensure that mortgages on homes supported by the AAH Program were financially sustainable for the family without creating undue barriers to homeownership for the low and moderate income families the program is designed to serve. These new underwriting standards are available for review upon request.

Comment 20

In addition, the internal review of the Department of Community Development conducted by the Chief of Regional Development has resulted in the introduction of an ordinance, now before Cleveland City Council, authorizing a major reorganization of the Department of Community Development. That reorganization will among other matters result in moving the AAH program to a larger program office consolidating various vacant house rehabilitation and homeownership programs. The internal review will take particular account of the final OIG report and findings before being finalized.

Comment 20

Finally, even though we believe that the income verification method used in Cleveland's AAH program meets or exceeds the guidelines provided by HUD, we are accepting the recommendation in the discussion draft. The City has already revised its income verification and income projection requirements. Beginning October 1, 2010, buyers assisted with second mortgage funds that have consistent incomes will need to provide three consecutive months of pay stubs to support income projections and confirm program eligibility. The revised policy and procedure is included in Appendix I. The revised policy also includes language for projecting income for families and individuals whose income is not consistent. We ask that HUD acknowledge the City's good faith efforts in making these changes and that if, after review, HUD determines that modifications to

Ref to OIG Evaluation **Auditee Comments**

the City's policies are needed that all activities administered between October 1, 2010 and the date of a final policy agreement by the City and HUD be accepted as complying with HOME income verification rules.

Ref to OIG Evaluation	Auditee Comments

Recommendation 1D: Review remaining 131 activities for sufficient income documentation and physical standard documentation.

Comment 21

Management Response – Agree: The City will review the balance of activities and determine the appropriateness of assistance provided in accordance with the response above. In the event that activities are identified where families are not income eligible using the methods outlined above, the City will take appropriate action. This review will be completed by July 31, 2011 and the files with documentation of the appropriate methodology will be available for inspection by HUD staff for each activity the City determines meets the Program guidelines for eligibility.

Ref to OIG Evaluation | **Auditee Comments**

Finding 2: The City lacked adequate controls over its afford-a-home program to ensure that appropriate recapture provisions were used for activities.

Comments 22 and 23

Management Response - Disagree: While the City acknowledges that the specific "net proceeds" language cited by the auditor was not in its loan documents, at no time did the City violate the 24 CFR 92.254 Program regulation which states that "when the recapture requirement is triggered by a sale (voluntary or involuntary) of the housing unit, and there are no net proceeds or the net proceeds are insufficient to repay the HOME investment due, the participating jurisdiction can only recapture the net proceeds, if any." The lack of specific "net proceeds" language had no substantive impact on Program outcomes.

- HOME assisted properties have gone to Sheriff's Sale, which resulted in the termination of the affordability period. This would have been true whether or not the City's documents contained the "net proceeds" provision.
- In no cases that we are aware of did a Sheriff's Sale result in any proceeds that exceeded the amount owed to the first mortgage holder. Had the "net proceeds" language been in the City documents, there still would have been no repayment to the homeowner or the City's HOME Program account.
- In conformance with 24 CFR 92.254, in no cases has the City taken legal action to require a foreclosed homeowner to repay HOME funds to the City from other sources.

Recommendation 2A – Reimburse its Program $30,000 from non-federal sources.

Management Response – Disagree: Finding #2 indicates that the City of Cleveland failed to include in its Annual Action Plans and Afford-A-Home Program documents, language that would limit the recapture of HOME funds to net proceeds, in the event of a foreclosure action. The City is being asked to reimburse its HOME account, from non-federal funds, the amount of HOME funds used to assist homes that have gone to Sheriff's Sale, resulting in a transfer of ownership.

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Ref to OIG Evaluation	Auditee Comments
Comment 22	While the City acknowledges that the specific "net proceeds" language was not in its documents, at no time were we aware that this could result in a potential financial liability. Had we known, we certainly would have made the required changes. Finding #2 cites 24 CFR 92.254 and information posted in the HOMEfires technical assistance section of the HUD website in June 2003 as primary sources for the requirement violated by the City.
Comment 22	The 24 CFR 92.254 program regulation states that "when the recapture requirement is triggered by a sale (voluntary or involuntary) of the housing unit, and there are no net proceeds or the net proceeds are insufficient to repay the HOME investment due, the participating jurisdiction can only recapture the net proceeds, if any." It also provides several options for restructuring recapture agreements. At no point does it indicate that the City's liability for repaying HOME funds on foreclosed properties will be determined by the inclusion of one specific provision in its loan documents. In compliance with the above regulation, the City has never taken legal action to require persons that have lost their homes through foreclosure to repay HOME funds in excess of net proceeds.
Comment 22	The 2003 HOMEfires web posting does describe the financial risks to a participating jurisdiction of not including the "net proceeds" language in its Program documents. To the best of our knowledge, no one on our staff was aware that this information had been made available at that time; nor have we seen or heard it explained in any recent HUD publications or training sessions, in spite of the national foreclosure crisis of the past few years.
Comment 22	After this issue was brought to our attention as the result of the February 1-3, 2010 Onsite Monitoring Review, new Program documents were developed that contain the language limiting the homeowner's and the City's financial liability to the available net proceeds, in the event of foreclosure. We believe that this is an appropriate corrective action. We do not agree that it is appropriate to require the City to reimburse its HOME Program account with money from its general fund resources. Page 16 of 19

Ref to OIG Evaluation **Auditee Comments**

An important factor to consider in determining whether the requested reimbursement is an appropriate course of action is the following question:

What was the actual programmatic or financial impact of the City's failure to include the required wording in its Program documents?

Comments 22 and 23

The reality is that there has been no substantive impact.

- HOME assisted properties have gone to Sheriff's Sale, which resulted in the termination of the affordability period. This would have been true whether or not the City's documents contained the "net proceeds" provision.
- In no cases that we are aware of did a Sheriff's Sale result in any proceeds that exceeded the amount owed to the first mortgage holder. Had the "net proceeds" language been in the City documents, there still would have been no repayment to the homeowner or the City's HOME Program account.
- In conformance with 24 CFR 92.254, in no cases has the City taken legal action to require a foreclosed homeowner to repay HOME funds to the City from other sources.

As stated in the HUD Columbus Office's July 2, 2010 Onsite Monitoring Review letter to the City:

HUD " adopted a policy (once a PJ adopted new recapture provisions that limited recapture to net proceeds and formally adopted a policy of not attempting to recapture amounts in excess of the net proceeds of a sale [this was in lieu of making the PJ go back and amend all its previous homebuyer agreements]) that HUD would not require PJ's to repay the entire amount of the HOME subsidy in the event that the net proceeds was less than the total subsidy"

The previously mentioned 2003 HOMEfires HUD web posting states:

"A PJ that was unaware that its homebuyer program design obligated it, in the event of foreclosure, to repay

Ref to OIG Evaluation **Auditee Comments**

> funds in excess of what would be available through the foreclosure and has changed the design to base recapture amounts on net proceeds may want to pursue a waiver of the repayment requirement at Section 92.503 (b) (1) for homeowners assisted under the original program design. HUD may grant a waiver on a program basis that, in the event of foreclosure involving homebuyers assisted under the previous program design, would limit the PJ's repayment obligation to the amount that it is able to obtain through the foreclosure."

Comment 22

The City was clearly unaware of the financial liability it was incurring by the failure to add the additional wording to its Program documents. We have now corrected the problem with respect to all future HOME homebuyer loans. On page 21 of our letter of July 30, 2010 to the HUD Columbus Field Office, in response to the Onsite Monitoring Review, we specifically requested the above referenced waiver of any past financial obligations resulting from this specific issue.

Finding # 2 also states that the City inappropriately indicated in its Action Plans that recaptured funds would be used to make additional loans to low income homebuyers.

The actual statement in the referenced Action Plans was:

> "The City will use the amount of the recapture to make additional loans to low-income homebuyers."

It was never our intent to imply that a specific dollar of recaptured Afford-A-Home funds would be held in our account until it could be specifically reused for another Afford-A-Home loan. The City fully complies with the HUD regulations at 24 CFR 92.502(c)(3) which require all program income and recaptured funds to be expended before additional HOME funds are requested from HUD.

The statement in our Action Plans was only to indicate our intent that the annual Afford-A-Home budget be supplemented by program income dollars in an amount that was at least equal to the amount of recaptured Afford-A-Home loan proceeds.

To avoid any misunderstanding, we will not include this statement in future Action Plans.

Recommendation 2B – Implement adequate procedures to ensure that if additional homes are transferred through foreclosure the net proceeds limitation will be implemented.

Management Response – Agree: As stated in response to the recommendation above, the City immediately implemented changes in its notes and mortgages when this issue was brought to its attention. As allowed by the 2003 HUD HOMEfires notice, we have requested a waiver of Program recapture of funds not available from net proceeds for mortgages and notes issued before the implementation date of April 1, 2010. It is impractical to exchange recorded notes and mortgages for all activities that might result in foreclosure. We request HUD's expedited approval of our waiver request and ask that the waiver cover all HOME second mortgages issued before April 1, 2010.

OIG's Evaluation of Auditee Comments

Comment 1 The City did not provide documentation to support that HUD found the City's method of calculating income eligibility for its Afford-A-Home program to be sufficient. The City's method of calculating income eligibility for its Afford-A-Home program was not reviewed as part of HUD's Office's 2006, 2007, or 2008 monitoring reviews of the City. Further, just because HUD's Office's 2006, 2007, and 2008 monitoring reviews of the City did not result in any findings or concerns regarding the City's calculations used to determine income eligibility, does not mean that HUD approved the City's calculations used to determine income eligibility.

Comment 2 Further, HUD's Office's February 2010 monitoring review identified that the City lacked sufficient documentation to support that households were income eligible and its calculations of households' annual income for activities. In addition, HUD's Office requested that we conduct an audit of the City's Afford-A-Home program due to the issues uncovered during its monitoring review.

Comment 3 The City did not provide documentation to support that it reimbursed its Program from non-Federal funds for the $10,000 in Program funds inappropriately used to assist activity number 10793 and removed activity number 10793 from HUD's System.

Comment 4 We revised the report to state the following:

- The City lacked sufficient documentation for 60 of the 71 activities reviewed to support that it used $760,000 in Program and/or Initiative funds for eligible households and/or activities.

- Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for 58 of the 71 activities reviewed were income eligible.

- The table in appendix D of this report shows the 60 activities for which the City did not have sufficient income documentation to demonstrate that households were income eligible and/or final inspection reports or certifications supporting that activities met HUD's property standards requirements at the time of occupancy.

- The City also lacked documentation to support its calculation of a household's annual income or that it calculated a household's annual income for two additional activities.

We also amended recommendation 1B to reflect these revisions.

In addition, we revised the table in Appendix D of this report by removing that the City had insufficient income documentation for activity numbers 10299, 10458, 10631, 10690, 10867, 10994, and 11087.

Comment 5 Chapter two of HUD's Technical Guide for Determining Income and Allowances for the Program, dated January 2005, states that a participating jurisdiction must project a household's future income by using the household's current income circumstances. The year-to-date pay statement, Internal Revenue Service form W-2 wage and tax statement, and/or tax return information may not reflect the household's current income circumstances.

Comment 6 Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for 32 of the 38 activities were income eligible.

Comment 7 Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for the 8 activities were income eligible.

Comment 8 Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for the 4 activities were income eligible.

Comment 9 Chapter two of HUD's Technical Guide for Determining Income and Allowances for the Program, dated January 2005, states that appropriate income documentation includes certified copies of tax returns. The tax returns provided by the City were not certified.

Comment 10 Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for the 2 activities were income eligible.

Comment 11 We revised the report to state the following:

- Contrary to HUD's regulations, the City drew down $20,000 in Program funds from October 14, 2008, through April 6, 2009, to assist two households that were not income eligible. The Program funds were used to provide interest-free second mortgage loans to the home buyers for activity numbers 10372 and 10793. The household income exceeded HUD's income guidelines by $9,406 (27 percent) for activity number 10793. The City could not provide sufficient income documentation for activity number 10372. However, it stated that the household was not income eligible.

We also amended recommendation 1A to reflect these revisions.

In addition, we revised the table in Appendix D of this report by removing that the City had insufficient income documentation for activity number 10372.

Comment 12 The City provided assistance for ineligible activities and lacked sufficient documentation to support that activities were eligible. As a result, it inappropriately provided $20,000 in Program funds to assist two households that were not income eligible and was unable to support its use of $760,000 in Program and/or Initiative funds.

Comment 13 Chapter two of HUD's Technical Guide for Determining Income and Allowances for the Program, dated January 2005, also states that a participating jurisdiction must project a household's future income by using the household's current income circumstances. Exhibit 2.1 states that a participating jurisdiction must include hourly wage figures, overtime figures, bonuses, anticipated raises, cost-of-living adjustments, or other anticipated changes in income in an applicant household's projected income calculation. For households with jobs providing steady employment, it can be assumed that there will only be slight variations in the amount of income earned. Therefore, 3 consecutive months' worth of income documentation is an appropriate amount upon which to base a household's projected income calculation for the following 12-month period. For those households with jobs providing employment that is less stable or does not conform to a 12-month schedule (e.g. seasonal laborers), income documentation that covers the entire previous 12-month period should be examined. In addition to hourly earnings, participating jurisdictions must account for all earned income. This income will include annual cost of living adjustments, bonuses, raises, and overtime pay in addition to base salary. In the case of overtime, it is important to determine whether overtime is sporadic or predictable. If a participating jurisdiction determines that a household will continue to earn overtime pay on a regular basis, it should calculate the average amount of overtime pay earned by the household over the past 3 months. This average should then be added to the total amount of projected earned income for the following 12-month period. Appropriate income documentation includes pay statements, third-party verification, bank statements, or certified copies of tax returns.

Comment 14 Contrary to HUD's requirements, the City lacked sufficient documentation to support that the households for the 12 activities were income eligible.

Comment 15 The City did not provide any policies or procedures that stated that developers provide specifications that show homes will meet or exceed local code standards upon completion of rehabilitation work or that closeout inspections verify that homes were in the same condition as they were in when the certificates of occupancy were signed.

Comment 16 The closeout inspection forms did not state that homes were in the same condition as they were in when the certificates of occupancy were signed.

Comment 17 The City's general specifications manual that it provided did not state that the specifications for rehabilitation work to be conducted on homes assisted with Program funds must cover all items needed for the homes to meet local codes.

Comment 18 HUD's regulations at 24 CFR 92.251(a)(2) state that housing acquired with Program funds must meet all applicable State and local housing quality standards and code requirements. HUD's regulations at 24 CFR 92.612(b) state that housing assisted with Initiative funds must meet the property standards in 24 CFR 92.251. Chapter five, part I, of HUD's "Building HOME: A Program Primer," dated March 2008, states that all housing quality standards and code requirements must be met at the time of occupancy. The City had certificates of occupancy stating that the nine homes met the City's building and zoning codes. However, the certificates of occupancy were dated from 193 to 1,036 days (at least 6 months) before the properties were purchased by the home buyers. Although the City had closeout inspection forms dated within 6 months of the properties' being purchased by the home buyers, the closeout inspection forms did not state that the homes met the City's building and zoning codes. Further, the City did not have documentation to support that the homes would meet the City's building and zoning codes when all of the work described in the rehabilitation specifications was finished. Therefore, the City lacked sufficient documentation to support that nine homes acquired with Program or Initiative funds met HUD's property standards requirements at the time of occupancy.

Comment 19 The City's revised final inspection form does not state that the home meets all applicable State and local housing quality standards and code requirements.

Comment 20 The City's commitment to new procedures and controls, if fully implemented, should improve the City's management of its Program.

Comment 21 The City's commitment to reviewing the remaining 131 activities to determine whether the households were income eligible and/or homes met HUD's property standards requirements at the time of occupancy, if fully implemented, should ensure that the City's Program is reimbursed from non-Federal funds for Program funds used for ineligible activities.

Comment 22 HUD's HOMEfires, volume 5, number 2, which has been in effect since June 2003, states that for Program-assisted home-buyer projects with recapture provisions, the amount of Program funds required to be repaid in the event of foreclosure is the amount that would be subject to recapture under the terms of the written agreement with the home buyer. If the recapture provisions require the entire amount of the Program investment from the home buyer, the amount required by the recapture provisions is the amount that must be recaptured by the participating jurisdiction for the Program. If the participating jurisdiction is unable to recapture the funds from the household, it must reimburse its Program in the amount due pursuant to the recapture provisions in the written agreement with the home buyer.

Comment 23 The City did not comply with HUD's requirements in its use of recapture provisions for activities. Neither the mortgages nor promissory notes between the City and the home buyers contained language that limited the amount of Program and/or Initiative funds the City could recapture to the net proceeds from the sale of a home. The mortgages and promissory notes required repayment of the full amount of the loan upon sale, lease, refinance, or transfer. The City did not implement appropriate recapture provisions for all 71 of the activities reviewed and did not ensure that its Program was reimbursed for Program funds used to assist home buyers in purchasing homes that were later sold through a sheriff's sale and ownership of the homes had been transferred. As a result, its Program was not reimbursed for $30,000 in Program funds used for three homes that were sold through a sheriff's sale and ownership of the homes had been transferred. Further, the City is at risk of being required to reimburse its Program additional non-Federal funds if the ownership of additional homes acquired under its Afford-A-Home program is transferred through foreclosure.

Appendix C

HUD’S REQUIREMENTS

Finding 1

HUD’s regulations at 24 CFR 92.2 define a low-income household as a household with an annual income that does not exceed 80 percent of the median income for the area as determined by HUD.

HUD’s regulations at 24 CFR 92.203(a) state that a participating jurisdiction must determine whether each household is income eligible by determining the household’s annual income. Section 92.203(a)(2) states that a participating jurisdiction must determine households’ annual income by examining source documentation evidencing households’ annual income. Section 92.203(d)(1) states a participating jurisdiction must calculate a household’s annual income by projecting the prevailing rate of the household’s income at the time the participating jurisdiction determines the household to be income eligible. Annual income shall include income from all household members.

HUD’s regulations at 24 CFR 92.217 state that a participating jurisdiction must invest Program funds made available during a fiscal year so that with respect to home ownership assistance, 100 percent of these funds are invested in dwelling units that are occupied by households that qualify as low-income households.

HUD’s regulations at 24 CFR 92.251(a)(2) state that housing acquired with Program funds must meet all applicable State and local housing quality standards and code requirements. If there are no such housing quality standards or code requirements, the housing must meet HUD’s housing quality standards.

HUD’s regulations at 24 CFR 92.508(a) state that a participating jurisdiction must establish and maintain sufficient records to enable HUD to determine whether it has met the requirements of 24 CFR Part 92. The participating jurisdiction must maintain records demonstrating the following:

- Each household is income eligible in accordance with 24 CFR 92.203.
- Each activity meets the property standards of 24 CFR 92.251.

HUD’s regulations at 24 CFR 92.602(a)(1) state that Initiative funds may only be used for downpayment assistance toward the purchase of single-family housing by low-income households that are first-time home buyers.

HUD’s regulations at 24 CFR 92.610(c) state that the income determination requirements in 24 CFR 92.203 apply to Initiative funds.

HUD's regulations at 24 CFR 92.612(b) state that housing assisted with Initiative funds must meet the property standards in 24 CFR 92.251.

HUD's regulations at 24 CFR 92.616(i) state that the record-keeping requirements in 24 CFR 92.508 apply to activities assisted with Initiative funds.

Chapter two, part I, of HUD's "Building HOME: A Program Primer," dated March 2008, states that income eligibility is based on anticipated income. Therefore, the previous year's tax return does not establish anticipated income and is not adequate source documentation. Chapter five, part I, states that all housing quality standards and code requirements must be met at the time of occupancy.

Chapter two of HUD's Technical Guide for Determining Income and Allowances for the Program, dated January 2005, states that a participating jurisdiction may develop its own income verification procedures provided that it collects source documentation and that this documentation is sufficient to enable HUD to monitor Program compliance. A participating jurisdiction must project a household's future income by using the household's current income circumstances. Exhibit 2.1 states that a participating jurisdiction must include hourly wage figures, overtime figures, bonuses, anticipated raises, cost-of-living adjustments, or other anticipated changes in income in an applicant household's projected income calculation. For households with jobs providing steady employment, it can be assumed that there will only be slight variations in the amount of income earned. Therefore, 3 consecutive months' worth of income documentation is an appropriate amount upon which to base a household's projected income calculation for the following 12-month period. For those households with jobs providing employment that is less stable or does not conform to a 12-month schedule (e.g. seasonal laborers), income documentation that covers the entire previous 12-month period should be examined. In addition to hourly earnings, participating jurisdictions must account for all earned income. This income will include annual cost of living adjustments, bonuses, raises, and overtime pay in addition to base salary. In the case of overtime, it is important to determine whether overtime is sporadic or predictable. If a participating jurisdiction determines that a household will continue to earn overtime pay on a regular basis, it should calculate the average amount of overtime pay earned by the household over the past 3 months. This average should then be added to the total amount of projected earned income for the following 12-month period. Appropriate income documentation includes pay statements, third-party verification, bank statements, or certified copies of tax returns.

Finding 2

Section 215(b) of Title II of the Cranston-Gonzalez National Affordable Housing Act, as amended, states that housing that is for home ownership shall qualify as affordable housing under Title II of the Act only if the housing is subject to resale restrictions that are established by the participating jurisdiction and determined by HUD's Secretary to be appropriate to (1) allow for the later purchase of the property only by a low-income household at a price which will provide the owner a fair return on investment and ensure that the housing will remain affordable to a reasonable range of low-income home buyers or (2) recapture the Program investment to assist other persons in accordance with the requirements of Title II of the Act, except when there are no net proceeds or when the net proceeds are insufficient to repay the full amount of the assistance.

HUD's regulations at 24 CFR 91.200(a) state that a complete consolidated plan consists of the information required in 24 CFR 91.220.

HUD's regulations at 24 CFR 91.220(1)(2)(ii) state that the action plan must include the guidelines for resale or recapture, as required in 24 CFR 92.254, if a participating jurisdiction intends to use Program funds for home buyers.

HUD's regulations at 24 CFR 92.254(a)(4) state that Program-assisted housing must meet the affordability requirements for not less than the applicable period beginning after activity completion. Home ownership activities that receive less than $15,000 in Program assistance must remain affordable for at least 5 years. Section 92.254(a)(5) states that to ensure affordability, a participating jurisdiction must impose either resale or recapture provisions that comply with the standards of section 92.254(a)(5) and include the provisions in its consolidated plan. Section 92.254(a)(5)(ii) states that a participating jurisdiction's recapture provisions must ensure that the participating jurisdiction recoups all or a portion of the Program assistance to the home buyers if the housing does not continue to be the principal residence of the household for the duration of the period of affordability. In establishing its recapture provisions, the participating jurisdiction is subject to the limitation that when the recapture provision is triggered by a voluntary or involuntary sale of the housing unit and there are no net proceeds or the net proceeds are insufficient to repay the Program investment due, the participating jurisdiction can only recapture the net proceeds, if any. The recaptured funds must be used to carry out Program-eligible activities in accordance with the requirements of 24 CFR Part 92.

HUD's regulations at 24 CFR 92.502(c)(3) state that a participating jurisdiction must disburse Program funds, including Program income and recaptured Program funds, in its local account before requesting Program funds from its treasury account. Section 92.503(c) states that Program funds recaptured in accordance with 24 CFR 92.254(a)(5)(ii) must be deposited in the participating jurisdiction's local account and used in accordance with the requirements of 24 CFR Part 92.

HUD's regulations at 24 CFR 92.612(c) state that housing assisted with Initiative funds must meet the affordability requirements in 24 CFR 92.254(a).

HUD's HOMEfires, volume 5, number 2, states that for Program-assisted home-buyer projects with recapture provisions, the amount of Program funds required to be repaid in the event of foreclosure is the amount that would be subject to recapture under the terms of the written agreement with the home buyer. If the recapture provisions provide for shared net proceeds, the amount subject to recapture is based on the amount of net proceeds, if any, from the foreclosure sale. If the recapture provisions require the entire amount of the Program investment from the home buyer or an amount reduced prorata based on the time the home buyer has owned and occupied the home measured against the affordability period, the amount required by the recapture provisions is the amount that must be recaptured by the participating jurisdiction for the Program. If the participating jurisdiction is unable to recapture the funds from the household, the participating jurisdiction must reimburse its Program in the amount due pursuant to the recapture provisions in the written agreement with the home buyer.

HUD's HOMEfires, volume 5, number 5, requires a participating jurisdiction to select either resale or recapture provisions for its Program-assisted home-buyer projects. The participating jurisdiction may select resale or recapture provisions for all of its home-buyer projects or resale or recapture provisions on a case-by-case basis. However, the participating jurisdiction must select whether resale or recapture will be imposed for each home-buyer project at the time the assistance is provided. A participating jurisdiction may adopt any one of four options in designing its recapture provisions. All of the options the participating jurisdiction will employ must be identified in its consolidated plan and approved by HUD.

Appendix D

SCHEDULE OF ACTIVITIES WITH INSUFFICIENT DOCUMENTATION

Activity number	*Income documentation*	*Final inspections or certifications*	*Assistance amount*
9852	X		$10,000
10075	X		20,000
10079	X		10,000
10093	X		10,000
10096	X		10,000
10109	X		10,000
10157	X		10,000
10161	X		10,000
10162	X	X	10,000
10163	X		10,000
10169	X		10,000
10171	X		10,000
10173	X	X	10,000
10174	X	X	10,000
10176	X		10,000
10229	X		10,000
10232	X	X	10,000
10289	X		10,000
10291	X		10,000
10301	X		10,000
10359	X		10,000
10360	X		10,000
10361	X		10,000
10362	X		10,000
10367	X		10,000
10368	X		10,000
10396	X		10,000
10420	X	X	10,000
10455	X		10,000
10457	X	X	10,000
10458		X	10,000
10634	X		10,000
10638	X	X	10,000
10686	X		10,000
10691	X		10,000
10769	X		20,000

SCHEDULE OF ACTIVITIES WITH INSUFFICIENT DOCUMENTATION (CONT.)

Activity number	Income documentation	Final inspections or certifications	Assistance amount
10771	X		20,000
10772	X		20,000
10773	X		20,000
10794	X		20,000
10796	X		10,000
10797	X		10,000
10802	X		10,000
10818	X		20,000
10821	X		10,000
10824	X		20,000
10846	X		10,000
10865	X		10,000
10866	X		20,000
10867		X	20,000
10868	X		10,000
10870	X		20,000
10888	X		20,000
10911	X		10,000
10961	X		20,000
10964	X		10,000
10991	X		10,000
10992	X		20,000
11073	X		20,000
11082	X		20,000
Totals	**58**	**9**	**$760,000**