HUD's Office of Multifamily Asset Management and Portfolio Oversight, Washington, DC

Low-Income Housing Preservation and Resident Homeownership Act of 1990

Office of Audit, Region 5
Chicago, IL

Audit Report Number: 2017-CH-0001
October 25, 2016

To:	Robert G. Iber, Acting Director of Multifamily Asset Management and Portfolio Oversight, HTN
	//signed//
From:	Kelly Anderson, Regional Inspector General for Audit, 5AGA
Subject:	HUD Needs To Improve Its Oversight of Funds Covered Under the Low-Income Housing Preservation and Resident Homeownership Act of 1990

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of HUD's oversight of funds covered under the Low-Income Housing Preservation and Resident Homeownership Act of 1990 in HUD's Line of Credit Control System.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at http://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at 312-353-7832.

Audit Report Number: 2017-CH-0001
Date: October 25, 2016

HUD Needs To Improve Its Oversight of Funds Under the Low Income Housing Preservation and Resident Homeownership Act of 1990

Highlights

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD) oversight of funds covered under the Low-Income Housing Preservation and Resident Homeownership Act of 1990 in HUD's Line of Credit Control System[1] based on information obtained during our audit of Carmen-Marine Apartments (2015-CH-1010). The audit was part of the activities in our fiscal year 2016 annual audit plan. Our objective was to determine whether HUD had adequate oversight of funds covered under the Act to ensure that the balances in the projects' grant accounts in HUD's System were appropriate.

What We Found

HUD did not ensure that (1) it remitted its share of the proceeds from initial sales associated with resident home-ownership program grants to the U.S. Treasury, (2) excess capital funds were deposited into the reserve for replacements accounts for the projects, and (3) authorized capital funds in the projects' grant accounts did not exceed the capital grant agreement amounts. As a result, (1) the U.S. Treasury did not have more than $1.2 million available for other appropriations, (2) HUD could not sufficiently support the use of more than $341,000 in proceeds from initial sales, and (3) six grantees did not have nearly $368,000 in capital funds in their projects' reserve for replacements accounts.

What We Recommend

We recommend that the Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight (1) coordinate with HUD's Office of the Chief Financial Officer to ensure that the proceeds are remitted to the U.S. Treasury, (2) coordinate with the appropriate HUD offices to provide sufficient documentation to support what HUD did with proceeds from initial sales, (3) deposit capital funds into the reserve for replacements accounts for six projects, and (4) implement adequate procedures and controls to ensure that future proceeds from initial sales paid to HUD are remitted to the U.S. Treasury.

---

[1] The System is HUD's primary grant disbursement system for handling disbursements for the majority of HUD programs. Grant disbursements are facilitated via the Internet through the System.

Table of Contents

Background and Objective

During the 1960s and 1970s, the U.S. Department of Housing and Urban Development (HUD) financed thousands of housing projects under its Federal Housing Administration (FHA) mortgage insurance programs. HUD insured loans for the projects for up to 40 years. However, it allowed owners to prepay the FHA-insured mortgage after 20 years and convert the projects to market-rate housing. This early prepayment option along with the expiration of project-based rental assistance contracts resulted in the loss of several hundred thousand affordable housing units. To prevent further loss of affordable housing units, Congress enacted the Low-Income Housing Preservation and Resident Homeownership Act in 1990. The Act imposed a general prepayment limitation of federally insured mortgages and offered owners fair-market-value incentives to (1) extend low-income affordability standards for the remaining useful life of the projects or (2) transfer the projects to nonprofit organizations, tenant associations, or community-based organizations that would keep the housing units affordable for the remaining useful life of the projects. The incentives included resident home-ownership program and capital grants. During fiscal years 1996 through 1998, Congress appropriated $987.5 million to HUD for properties eligible for assistance under the Act or the Emergency Low-Income Housing Preservation Act of 1987. Congress has not appropriated funds to HUD for properties eligible for assistance under the Act since 1998. As of November 2012, HUD oversaw an inventory of approximately 640 projects and more than 75,000 units subject to provisions of the Act.[2]

During an audit of Carmen-Marine Apartments (2015-CH-1010), we identified nearly $312,000 in proceeds from initial membership sales in its grant account in HUD's Line of Credit Control System. As of January 2016, we identified 17 projects, including Carmen-Marine Apartments, with nearly $1.6 million in funds in the projects' grant accounts in HUD's System[3] and selected for review nine projects with a balance of more than $50,000. As of May 2016, the balances for the nine projects totaled more than $1.5 million.

HUD awarded the (1) 707 Tenants' Association for Lakeview East Cooperative in Chicago, IL, (2) Carmen-Marine Tenants' Association for Carmen-Marine Apartments in Chicago, IL, and (3) West Park Place Residents Association for Preservation for West Park Place Condominium in Chicago, IL, grants of more than $56 million through its program under the Act.[4] The grantees were required to use the program and capital funds to acquire and rehabilitate the projects and transfer ownership of the projects' units to a cooperative or condominium form of ownership, which would then sell memberships in the cooperative or the project's units, as appropriate, to tenants in occupied units. The cooperative or condominium ownership entities were required to remit to HUD 50 percent of

[2] This information came from HUD's Housing Notice 2012-25, dated November 21, 2012.
[3] As of May 2016, the balances for the 17 projects totaled more than $1.6 million due to more than $48,000 in proceeds from initial sales being remitted to HUD since January 2016.
[4] HUD's program grant agreement with the 707 Tenants' Association for Lakeview East Cooperative included more than $6.5 million in capital funds. This was the only program grant agreement that included capital funds.

the proceeds from initial membership or unit sales. HUD was required to use its share of the proceeds from initial sales for eligible assistance under the Act and HUD's regulations. HUD's Chicago Multifamily Housing Hub had monitoring responsibility for the three projects.

HUD awarded (1) Floral Gardens Apartments Incorporated for Floral Gardens Apartments in Selma, CA, (2) Cedar Gardens Apartments for Cedar Gardens Apartments in Fresno, CA, (3) Fountain West Apartments Incorporated for Fountain West Apartments in Fresno, CA, (4) Prince Hall of Bethel A.M.E. Church Incorporated for Prince Hall Apartments in San Francisco, CA, (5) Keller Housing Initiatives Incorporated for Keller Plaza Apartments in Oakland, CA, and (6) Fredericksburg Non-Profit Housing Corporation for Apartments Northwest in San Antonio, TX, nearly $28 million in capital grants under the Act. The grantees were required to use the capital funds to acquire and rehabilitate the projects. HUD's San Francisco Multifamily Housing Hub had monitoring responsibility for the five projects in California, and HUD's Fort Worth Multifamily Housing Hub had monitoring responsibility for the project in Texas.

The following table shows for the nine projects, the type (program or capital) and date of the grant agreement HUD awarded and the fund balances in the projects' grant accounts.

Project	Program	Capital	Date	Authorized	Disbursed	Balance
Lakeview East Cooperative	X		Aug. 1996	$18,756,339	$18,357,849	$398,490
Carmen-Marine Apartments	X		Jan. 1994	23,104,550	22,792,603	311,947
Floral Gardens Apartments		X	Aug. 1996	2,482,729	2,236,914	245,815
West Park Place Condominium	X		May 1995	14,183,850	13,961,137	222,713
Cedar Gardens Apartments		X	Nov. 1995	5,905,062	5,806,730	98,332
Fountain West Apartments		X	Aug. 1996	3,208,282	3,114,283	93,999
Prince Hall Apartments		X	Sept. 1996	7,066,866	7,003,408	63,458
Keller Plaza Apartments		X	Sept. 1996	7,460,571	7,398,184	62,387
Apartments Northwest		X	Dec. 1995	2,099,411	2,049,030	50,381
Totals	**3**	**6**		**$84,267,660**	**$82,720,138**	**$1,547,522**

HUD's Office of Multifamily Asset Management and Portfolio Oversight had oversight responsibility for projects subject to the provisions of the Act. It relied on HUD's regional and field Offices of Multifamily Housing Programs to monitor the projects.

Our objective was to determine whether HUD had adequate oversight of funds covered under the Act to ensure that the balances in the projects' grant accounts in HUD's System were appropriate. Specifically, we wanted to determine whether HUD (1) remitted its share of the proceeds from initial sales associated with program grants to the U.S. Treasury, (2) ensured that grantees deposited excess capital funds into the reserve for replacements accounts for the projects, and (3) authorized capital funds in the projects' grant accounts in excess of the capital grant agreement amounts.

Results of Audit

Finding: HUD's Oversight of Proceeds From Initial Sales and Undisbursed Program and Capital Funds Had Weaknesses

HUD did not ensure that (1) it remitted its share of the proceeds from initial sales associated with program grants to the U.S. Treasury, (2) excess capital funds were deposited into the reserve for replacements accounts for the projects, and (3) authorized capital funds in the projects' grant accounts did not exceed the capital grant agreement amounts. These deficiencies occurred because HUD had weaknesses in its procedures and controls over proceeds from initial sales and program and capital funds. As a result, (1) the U.S. Treasury did not have more than $1.2 million available for other appropriations, (2) HUD could not sufficiently support the use of more than $341,000 in proceeds from initial sales, and (3) six grantees did not have nearly $368,000 in capital funds in their reserve for replacements accounts for the projects.

Proceeds From Initial Sales Were Not Remitted to the U.S. Treasury

For the three projects for which grantees received program grants,[5] we reviewed the proceeds from initial sales to determine whether HUD remitted its share of the proceeds to the U.S. Treasury. Based on the three projects' audited financial statements for the fiscal years 1998 through 2015, nearly $1.1 million in proceeds was remitted to HUD. Further, more than $72,000 in proceeds had been remitted to HUD for West Park Place Apartments (more than $48,000) and Carmen-Marine Apartments (more than $24,000) since the projects' fiscal year 2015. HUD's Office of the Chief Financial Officer's Fort Worth Accounting Center's Receipt and Disbursement Information System supported that HUD had received payments for all but just over $2,000 of the nearly $1.2 million (nearly $1.1 million + more than $72,000) in proceeds reported as remitted to HUD (1) in the projects' audited financial statements or (2) since the projects' fiscal year 2015.

HUD did not remit its share of proceeds from initial sales to the U.S. Treasury.

Contrary to section 226(b)(4) of the Act and HUD's regulations at 24 CFR (Code of Federal Regulations) 248.173(h), HUD inappropriately deposited the following sale proceeds:

- $757,028 into the projects' program grant accounts in HUD's System.
- $110,858 into a preservation technical assistance grant account in HUD's System associated with Carmen-Marine Apartments. In August 2013, the initial two deposits of

[5] 707 Tenants' Association for Lakeview East Cooperative, Carmen-Marine Tenants' Association for Carmen-Marine Apartments, and West Park Place Residents Association for Preservation for West Park Place Condominium.

proceeds totaling $43,582 were deauthorized from the account. HUD's Deputy Assistant Chief Financial Officer for Systems said that the nearly $44,000 in proceeds was transferred to HUD's housing certificate fund account, which was the fund that contained the appropriations for the program grants. However, HUD had not provided sufficient documentation to support that the nearly $44,000 in proceeds was transferred to the housing certificate fund account. As of July 2016, the balance in the grant account was $67,276.

Further, based on the Accounting Center's System, HUD deposited the following proceeds: (1) $271,107 into two of HUD's miscellaneous receipts accounts to be returned to the U.S. Treasury, (2) $18,235 into HUD's Home-Ownership and Opportunity for People Everywhere grants account, and (3) $8,306 into a HUD clearing account to be transferred to FHA. However, HUD had not provided sufficient documentation to support that these deposits occurred.

The table in appendix D of this report summarizes the results of our review of the proceeds from initial sales.

The Director of the Accounting Center stated that he would communicate with HUD's Office of Multifamily Housing Programs to ensure that the proceeds remitted to HUD were treated appropriately.

Undisbursed Program and Capital Funds Were Used To Offset Proceeds From Initial Sales
Contrary to articles V(e) and XIII of HUD's program grant agreement with the 707 Tenants' Association for Lakeview East Cooperative, HUD did not ensure that the Association deposited $148,872 in excess capital funds into the reserve for replacements account for the project. The Association used the excess capital funds in the project's grant account in HUD's System to offset proceeds from initial sales that were to be remitted to HUD. Since the excess capital funds were to be deposited into the reserve for replacements account for the project, we considered the nearly $149,000 in the project's grant account to be proceeds from initial sales. The Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight agreed that the nearly $149,000 in excess capital funds in the project's grant account should have been deposited into the reserve for replacements account for the project and that it should now be considered proceeds from initial sales.

Contrary to section 226(b)(4) of the Act, regulations at 24 CFR 248.173(h), and article IV(j) of HUD's program grant agreement with the West Park Place Residents Association for Preservation for West Park Place Condominium,[6] HUD did not ensure that the West Park Place Condominium Association did not use $27,250 in undisbursed program funds in the project's grant account in HUD's System to offset proceeds from initial sales that were to be remitted to HUD. The Director of HUD's Multifamily Midwest Region said that the program funds were to be used during the conversion to home ownership period. Therefore, it was not appropriate for the Condominium Association to use the undisbursed program funds to offset the proceeds and

[6] The program grant agreement did not address excess program funds.

HUD's Chicago Multifamily Housing Hub would not have approved it. Further, HUD's Chicago Multifamily Housing Hub's position was that the more than $27,000 in undisbursed program funds needed to be deauthorized from the project's grant account and remitted to the U.S. Treasury.

Capital Funds Were Not Deposited Into Reserve for Replacements Accounts

For the six projects for which grantees received capital grants,[7] we reviewed the capital funds in the projects' grant accounts to determine whether the funds were excess capital funds that were not deposited into the reserve for replacements accounts for the projects.

Contrary to articles VI.C. and VIII of HUD's capital grant agreements with the grantees for six projects, HUD did not ensure that the grantees deposited $367,645 in excess capital funds into the projects' reserve for replacements accounts. The Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight agreed that the nearly $368,000 should have been and needed to be deposited into the accounts. As a result of our audit, HUD's staff in its San Francisco and Fort Worth Multifamily Housing Hubs was working on getting the funds deposited into the accounts.

Authorized Capital Funds Were in Excess of Grant Agreement Amounts

For the six projects for which grantees received capital grants,[8] we reviewed the capital funds in the projects' grant accounts to determine whether the funds were authorized capital funds in the projects' grant accounts in excess of the capital grant agreement amounts.

Contrary to article I.A. of HUD's capital grant agreements with Floral Gardens Apartments, Inc., for Floral Gardens Apartments and Fountain West Apartments, Inc., for Fountain West Apartments, HUD authorized $246,727 ($187,792 for Floral Gardens Apartments + $58,935 for Fountain West Apartments) in capital funds in the projects' grant accounts in HUD's System in excess of the grant agreement amounts. A project manager in HUD's San Francisco Multifamily Housing Hub stated that there were no amendments to the capital grant agreements that increased the capital funds awarded for the two projects. The Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight stated that the nearly $247,000 in capital funds in the projects' grant accounts in excess of the grant agreement amounts could be remitted to the U.S. Treasury.

> Excess capital funds were in the projects' grant accounts in HUD's System for nearly 20 years.

[7] Floral Gardens Apartments Incorporated for Floral Gardens Apartments, Cedar Gardens Apartments for Cedar Gardens Apartments, Fountain West Apartments Incorporated for Fountain West Apartments, Prince Hall of Bethel A.M.E. Church Incorporated for Prince Hall Apartments, Keller Housing Initiatives Incorporated for Keller Plaza Apartments, and Fredericksburg Non-Profit Housing Corporation for Apartments Northwest

[8] See list in footnote 7.

HUD Had Weaknesses in Procedures and Controls Over Funds Covered Under the Act

The deficiencies described above occurred because HUD had weaknesses in its procedures and controls over funds covered under the Act to ensure that (1) its share of the proceeds from initial sales associated with program grants were remitted to the U.S. Treasury and (2) undisbursed program and capital funds were not inappropriately in the projects' grant accounts in HUD's System.

HUD's Office of Multifamily Asset Management and Portfolio Oversight had oversight responsibility for projects subject to the provisions of the Act. It relied on HUD's regional and field Offices of Multifamily Housing Programs to monitor the projects. Further, HUD's Deputy Assistant Chief Financial Officer for Systems said that HUD's Office of the Chief Financial Officer performed an open obligations review each year. The Office identified accounts in HUD's System with open obligations. It then requested HUD's program offices to review the open obligations for which the offices were responsible. He then retained, deobligated, or recaptured obligations based on the offices' responses.

HUD's Office of Multifamily Housing Programs did not provide HUD's Office of the Chief Financial Officer's Fort Worth Accounting Center guidance or instructions and the Director of the Accounting Center said that he did not know whether staff from the Accounting Center contacted the Office regarding how to handle proceeds from initial sales remitted to HUD. Further, staff in HUD's Chicago Multifamily Housing Hub responsible for monitoring the projects associated with the program grants did not review the projects' program grant accounts or the payments to HUD for its share of the proceeds. The Director of HUD's Multifamily Midwest Region said that it was his understanding that HUD's Real Estate Assessment Center was responsible for reviewing the projects' audited financial statements and ensuring that the appropriate amount of proceeds was remitted to HUD. A supervisory auditor with the Real Estate Assessment Center stated that the Center's review of the projects' audited financial statements normally would not include the proceeds. The Director also said that he was not sure whether the projects' grant accounts were included in the open obligations provided by the Office of the Chief Financial Officer. However, he said that it was possible that the projects' grant accounts were included as open obligations, and HUD's Chicago Multifamily Housing Hub responded that the obligations should be retained since it had not been provided sufficient time to review the hundreds of open obligations under its responsibility.

Staff in HUD's San Francisco and Fort Worth Multifamily Housing Hubs currently responsible for monitoring the projects associated with the capital grants was not the staff responsible for monitoring the projects when the capital funds were drawn down. Further, HUD files for the projects contained limited information regarding the history of the projects. Therefore, the staff could not explain why (1) excess capital funds were not deposited into the reserve for replacements accounts for the projects or (2) HUD had authorized capital funds in the projects' grant accounts in HUD's System in excess of the grant agreement amounts. The staff also either did not have access to or had limited access in HUD's System to be able to see that there were undisbursed capital funds in the projects' grant accounts. In addition, the staff stated that it had not seen correspondence from the Office of the Chief Financial Officer concerning open obligations.

Conclusion

HUD needs to improve its procedures and controls over funds covered under the Act to ensure that (1) its share of the proceeds from initial sales associated with program grants was remitted to the U.S. Treasury and (2) undisbursed program and capital funds were not inappropriately in the projects' grant accounts in HUD's System. As a result, the U.S. Treasury did not have $1,247,153 available for additional appropriations.[9] Further, HUD could not sufficiently support what it did with $341,230 in proceeds from initial sales.[10] In addition, six grantees did not have nearly $368,000 in capital funds in their reserve for replacements accounts for the projects.

Recommendations

We recommend that the Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight

1A. Deobligate the $1,247,153 in proceeds from initial sales associated with program grants and undisbursed program and capital funds, and coordinate with HUD's Office of the Chief Financial Officer to ensure that the proceeds are remitted to the U.S. Treasury.

1B. Coordinate with the appropriate HUD offices to provide sufficient documentation to support what HUD did with $341,230 in proceeds from initial sales. If any proceeds were not remitted to the U.S. Treasury, coordinate with the appropriate offices to ensure that the proceeds are remitted to the U.S. Treasury.

1C. Deposit the $367,645 in capital funds into the reserve for replacements accounts for the six projects.

1D. Review the remaining eight projects with $79,735 in the projects' grant accounts (17 projects with more than $1.6 million in the projects' grant accounts – nine projects reviewed with more than $1.5 million in the projects' grant accounts) and determine whether it is appropriate for the funds to be in the projects' grant accounts. If the funds should not be in the projects' grant accounts, HUD should take the proper corrective actions.

---

[9] The more than $1.2 million consisted of more than $757,000 in proceeds from initial sales in the projects' program grant accounts + more than $67,000 in proceeds from initial sales in a preservation technical assistance grant account associated with Carmen-Marine Apartments + nearly $149,000 in undisbursed capital funds in Lakeview East Cooperative's program grant account that was used to offset proceeds + more than $27,000 in undisbursed program funds in West Park Place Condominium's program grant account that was used to offset proceeds + nearly $247,000 in capital funds in two projects' capital grant accounts in excess of the grant agreement amounts.

[10] The more than $340,000 consisted of nearly $44,000 in proceeds deauthorized from the preservation technical assistance grant account associated with Carmen-Marine Apartments + more than $271,000 deposited into two of HUD's miscellaneous receipts accounts to be returned to the U.S. Treasury based on the Accounting Center's System + more than $18,000 deposited into HUD's Home-Ownership and Opportunity for People Everywhere grants account based on the Accounting Center's System + more than $8,000 deposited into a HUD clearing account to be transferred to FHA based on the Accounting Center's System.

1E. Implement adequate procedures and controls to ensure that proceeds from initial sales paid to HUD are remitted to the U.S. Treasury.

Scope and Methodology

We performed our audit work from January through August 2016 at HUD's Chicago regional office located at 77 West Jackson Boulevard, Chicago, IL. The audit covered the period November 1990 through December 2015 and was expanded as necessary.

To accomplish our objective, we reviewed

- Applicable laws; regulations at 24 CFR Part 248; HUD's grant and use agreements with the grantees; and Office of Inspector General (OIG) audit reports 2015-FO-0002, issued December 8, 2014, 2015-CH-1010, issued September 30, 2015, and 2016-FO-0003, issued November 18, 2015.

- The projects' audited financial statements for the fiscal years 1998 through 2015, resident home-ownership plans, and plans of action as applicable.

- Data in HUD's System and the Accounting Center's System.

In addition, we interviewed HUD staff.

In January 2016, HUD provided a list of projects awarded a preservation resident home-ownership grant from HUD's System subject to provisions of the Act. The list included 201 projects with nearly $683.9 million reserved, obligated, and contracted and nearly $682.3 million disbursed. The list also included 17 projects with nearly $1.6 million in undisbursed funds. We selected a nonrepresentative sample of nine projects with a balance of more than $50,000 in the projects' grant accounts in HUD's System to determine whether HUD (1) remitted its share of the proceeds from initial sales associated with program grants to the U.S. Treasury, (2) ensured that grantees deposited excess capital funds into the reserve for replacements accounts for the projects, and (3) authorized capital funds in the projects' grant accounts in excess of the capital grant agreement amounts. The balances for the nine projects totaled more than $1.5 million. We used a nonrepresentative sample since we knew enough about the population to identify a relatively small number of accounts with large balances that included nearly all of the $1.6 million in funds and we were not projecting the results to the population that we did not review.

We relied on the data from HUD's System and the Accounting Center's System. Although we did not perform a detailed assessment of the reliability of the data, we performed minimal levels of testing and found the data to be adequately reliable for our purposes.

We provided the results of our audit to the Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight during the audit. We asked the Acting Director to provide written comments on our discussion draft audit report by September 20, 2016. The Acting Director of HUD's Office of Multifamily Asset Management and Portfolio Oversight decided to not comment on the draft report.

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

Internal Controls

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the 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 objective:

- 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 or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiency

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

- HUD had weaknesses in its procedures and controls over funds covered under the Act to ensure that (1) its share of the proceeds from initial sales associated with program grants was remitted to the U.S. Treasury and (2) undisbursed program and capital funds were not inappropriately in the projects' grant accounts in HUD's System (finding).

Appendixes

Appendix A

Schedule of Questioned Costs and Funds To Be Put to Better Use[11]

Recommendation number	Unsupported 1/	Funds to be put to better use 2/
1A		$186,039
1B	$341,230	
Totals	**$341,230**	**$186,039**

1/ 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 legal interpretation or clarification of departmental policies and procedures.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, implementation of our recommendation will ensure that HUD remits proceeds from initial sales associated with program grants to the U.S. Treasury.

[11] As part of OIG's financial statement audits of HUD, the Financial Audits Division included nearly $1.5 million of the more than $1.6 million in the projects' grant accounts in HUD's System for the 17 projects and nearly $22,000 of the more than $67,000 in the preservation technical assistance grant account associated with Carmen-Marine Apartments as inactive, expired, or no longer needed obligations that HUD needed to either deobligate or review and if necessary, deobligate (see finding 6 in OIG audit report 2015-FO-0002 issued December 8, 2014, and finding 8 in OIG audit report 2016-FO-0003, issued November 18, 2015). However, HUD previously reported that the grants for the 17 projects were active and the funds were not to be deobligated and that it did not review the amount in the preservation technical assistance grant account associated with Carmen-Marine Apartments. Therefore, we did not include as funds to be put to better use $1,061,114 ($1,039,515 that OIG's Financial Audits Division reported in its financial statement audits of HUD for the nine projects' grant accounts + $21,599 that OIG's Financial Audits Division reported in its financial statement audit of HUD for the preservation technical assistance grant account associated with Carmen-Marine Apartments) of the more than $1.2 million in proceeds from initial sales associated with program grants and undisbursed program and capital funds that was included in recommendation 1A and the nearly $368,000 in capital funds that was not deposited into the reserve for replacements accounts for six projects that were included in recommendation 1C.

Appendix B

Applicable Requirements

Section 226(b)(4) of the Act states that the entity that transfers ownership interests in or shares representing units to eligible households may use 50 percent of the proceeds from the initial sale for costs of the program, including improvements to the project, operating and replacement reserves for the project, additional home-ownership opportunities in the project, and other project-related activities approved by HUD. The remaining 50 percent of the proceeds must be returned to HUD for use under section 220 of the Act, subject to the availability of appropriations. The entity must keep and make available to HUD all records necessary to accurately calculate payments due to HUD.

Regulations at 24 CFR 248.173(h) state that the entity that transfers ownership interests in or shares representing units to eligible households may use 50 percent of the proceeds from the initial sale for costs of the program, including improvements to the project, operating and replacement reserves for the project, additional home-ownership opportunities in the project, and other project-related activities approved by HUD. The remaining 50 percent of the proceeds must be returned to HUD for use under 24 CFR 248.157 and 248.161, subject to the availability of appropriations. The entity must keep and make available to HUD all records necessary to accurately calculate payments due to HUD.

Article V(e) of HUD's program grant agreement with the 707 Tenants' Association for Lakeview East Cooperative states that the 707 Tenants' Association agrees that any excess funds must be deposited into the reserve for replacements account for the project. Article XIII states that if the total amount of funds allocated to the project under the grant agreement was not spent, the 707 Tenants' Association must deposit any excess amount into the reserve for replacements account established for the project.

Article IV(j) of HUD's program grant agreement with the West Park Place Residents Association for Preservation for West Park Place Condominium states that at the time of the sales of units to the initial owners, the West Park Place Condominium Association must remit to HUD 50 percent of all proceeds from the unit sales. If cash is received from the initial owner because the owner receives a loan for the purchase price, 50 percent of the cash received must be remitted to HUD. If the Condominium Association provides the mortgage loan to the owner, the Condominium Association must remit to HUD 50 percent of the principal paid by the owner as it is paid to the Condominium Association. If the initial owner transfers the unit to a subsequent purchaser who assumes the initial owner's remaining debt, 50 percent of the principal amount collected will continue to be remitted to HUD.

Article VI.C. of HUD's capital grant agreements with the grantees for the six projects states that the grantees agree that any excess capital funds must be deposited into the reserve for replacements accounts for the projects. Article VIII states that if the total amount of capital funds allocated to the projects under the grant agreements was not spent, the grantees must deposit any excess amounts into the reserve for replacements accounts established for the projects.

Article I.A. of HUD's capital grant agreements with Floral Gardens Apartments, Inc., for Floral Gardens Apartments states that HUD agreed to provide and Floral Gardens Apartments, Inc., agreed to accept $2,294,937 in capital funds under the Act. Article I.A. of HUD's capital grant agreement with Fountain West Apartments, Inc., for Fountain West Apartments states that HUD agreed to provide and Fountain West Apartments, Inc., agreed to accept $3,149,347 in capital funds under the Act.

Appendix C

Schedule of Proceeds From Initial Sales

Project	Recorded in the Accounting Center's System	In program grant accounts	In preservation technical assistance grant account	In HUD's housing certificate account	Returned to the U.S. Treasury	In Home-Ownership for People Everywhere grants account	Transferred to FHA
Lakeview East Cooperative	$425,110	$249,618			$167,186		$8,306
Carmen-Marine Apartments	461,912	311,947	$67,276	$43,582	20,872	$18,235	
West Park Place Condominium	278,512	195,463			83,049		
Totals	$1,165,534	$757,028	$67,276	$43,582	$271,107	$18,235	$8,306