Lexington-Fayette Urban County Housing Authority, Lexington, KY

Rental Assistance Demonstration Program
Section 8 Project-Based Voucher Program

Office of Audit, Region 4
Atlanta, GA

Audit Report Number: 2018-AT-1008
July 13, 2018

To: Carol C. Spencer, Director, Public and Indian Housing, Louisville, KY, Field Office, 41PH

//**Signed**//

From: Nikita N. Irons, Regional Inspector General for Audit, 4AGA

Subject: The Lexington-Fayette Urban County Housing Authority, Lexington, KY, Did Not Fully Comply With HUD's Program Requirements After the Completion of Its Rental Assistance Demonstration Program Conversion

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Lexington-Fayette Urban County Housing Authority's Section 8 Project-Based Voucher program after the Rental Assistance Demonstration Program conversion.

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 website. 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 404-331-3369.

Audit Report Number: 2018-AT-1008
Date: July 13, 2018

The Lexington-Fayette Urban County Housing Authority, Lexington, KY, Did Not Fully Comply With HUD's Program Requirements After the Completion of Its Rental Assistance Demonstration Program Conversion

Highlights

What We Audited and Why

We audited the Lexington-Fayette Urban County Housing Authority's Rental Assistance Demonstration Program (RAD) conversion to the Section 8 Project-Based Voucher program and compliance with requirements after the conversion. We selected the Authority for review in accordance with our annual audit plan. Our audit objective was to determine whether the Authority complied with the U.S. Department of Housing and Urban Development's (HUD) program requirements for conducting unit inspections and rent reasonableness determinations after RAD conversion.

What We Found

After its RAD conversion, the Authority did not fully comply with HUD's program requirements for conducting unit inspections and rent reasonableness determinations. Specifically, the Authority did not obtain the services of a HUD-approved independent entity for conducting unit inspections in compliance with HUD's housing quality standards and rent reasonableness determinations for units it owned. This condition occurred because the Authority initially did not realize that the independent entity inspections for housing quality standards and rent reasonableness determinations requirements remained applicable after the RAD conversion although the rents were set by HUD and the units were substantially rehabilitated. As a result, the Authority inappropriately paid more than $394,000 in housing assistance payments and received more than $49,000 in administrative fees. In addition, HUD and the Authority lacked assurance that the unit inspections and rent reasonableness determinations were properly conducted.

What We Recommend

We recommend that the Director of HUD's Louisville, KY, Office of Public and Indian Housing require the Authority to (1) reimburse its appropriate programs more than $443,000 from nonproject funds for inappropriately conducting unit inspections and rent reasonableness determinations on units it owned and (2) coordinate with HUD and provide adequate training to its staff to ensure compliance with HUD's requirements.

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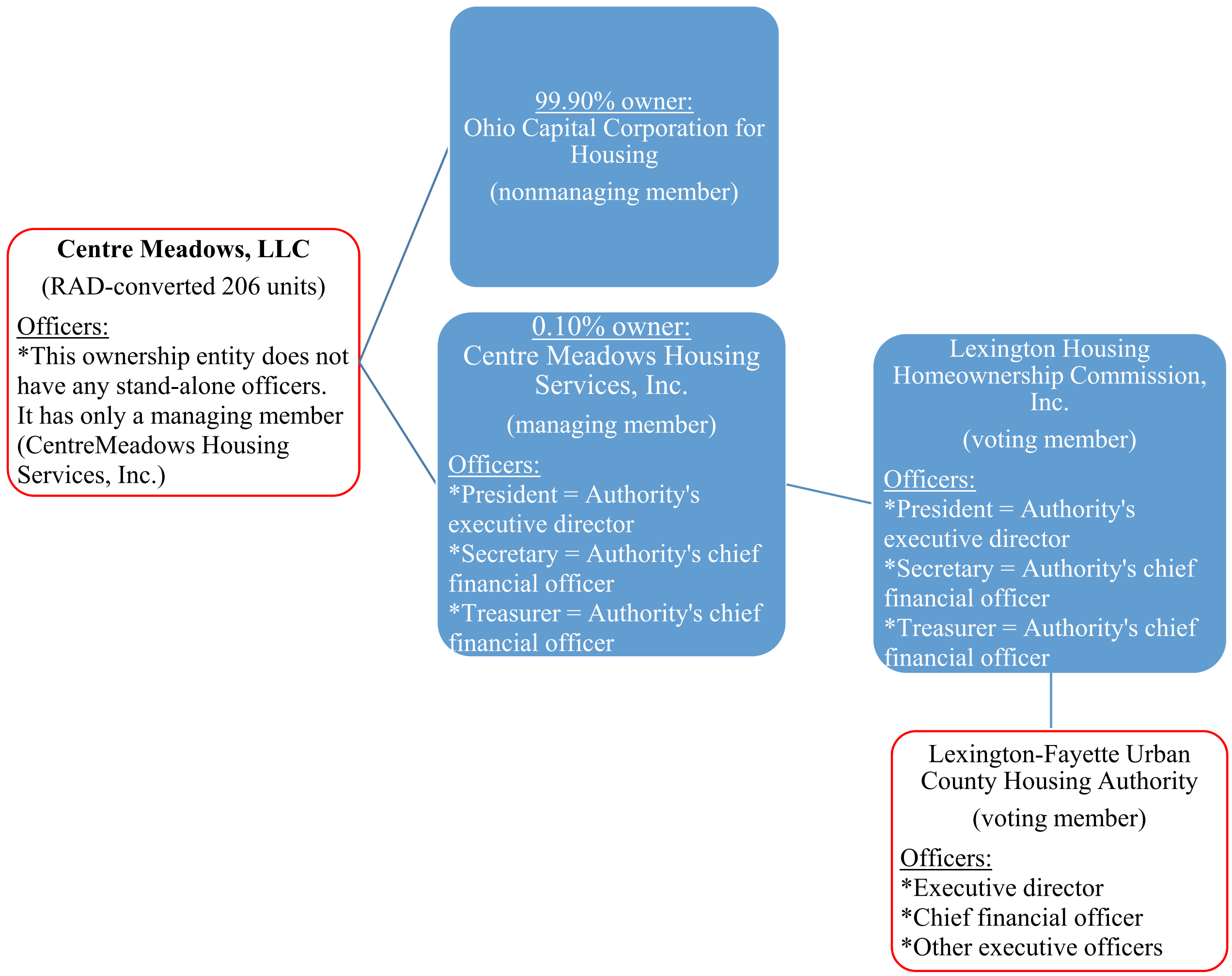
Background and Objective

Established under the State of Kentucky's Municipal Housing Commission Act of 1934, the Lexington-Fayette Urban County Housing Authority came into its current form after a merger between the City of Lexington and Fayette Urban County in April 1970 and a name change in March 1974. The Authority is governed by a five-member board of commissioners and an executive director. The Authority's mission is to provide safe and desirable housing to low- and moderate-income individuals and families while partnering with other agencies to enhance its community involvement and self-sufficiency and a higher quality of life for its residents.

The Rental Assistance Demonstration Program (RAD) was authorized in fiscal year 2012 to preserve and improve public housing properties and address a $26 billion nationwide backlog of deferred maintenance. RAD's purpose is to provide an opportunity to test the conversion of public housing and other U.S. Department of Housing and Urban Development (HUD)-assisted properties to long-term, project-based Section 8 rental assistance properties to achieve certain goals, including preserving and improving these properties by enabling public housing agencies to use private debt and equity to address immediate and long-term capital needs. RAD has two components. The first component allows the conversion of public housing and moderate rehabilitation properties to properties with long-term project-based Section 8 rental assistance contracts. The second component allows rent supplement, rental assistance payments, and moderate rehabilitation properties to convert tenant protection vouchers to project-based assistance at the end of the contract. The Authority used the first component of RAD and had converted 206 of its 1,303 public housing units at its Pimlico Apartments project to 206 Section 8 Project-Based Voucher units in the newly named Centre Meadows Apartments as of March 4, 2014. The Authority had 1,097 units remaining in its public housing portfolio following this RAD conversion. The Authority was recognized by HUD as having the first RAD transaction with a Federal Housing Administration mortgage insurance for new construction or substantial rehabilitation of rental housing.

The Authority owned all 206 units converted under RAD. Specifically, the Authority was the sole voting member of one subsidiary, which in turn was the sole voting member of another entity that had 0.10 percent ownership stake in the project, Centre Meadows Apartments. In addition, the subsidiaries and the Authority had some staff members in common. Specifically, the Authority's executive director and the chief financial officer served both as the Authority's officers and officers of the subsidiary entities of the Centre Meadows Apartments project. Further, HUD defined Authority-owned units at 24 CFR (Code of Federal Regulations) 983.3(b) as units for which the Authority or its officers, employees, or agents held a direct or indirect interest in the building in which the unit was located, including an interest as titleholder or lessee or as a stockholder, member or general or limited partner, or member of a limited liability corporation or an entity that held any such direct or indirect interest. The chart below illustrates the ownership and staffing relationship between the Authority and Centre Meadows Apartments.



In addition, the Authority had participated in HUD's Moving-to-Work (MTW) demonstration since November 2011. Under MTW, public housing agencies are provided the opportunity to design and test innovative, locally designed strategies that use Federal dollars more efficiently, help residents find employment and become self-sufficient, and increase housing choices for low-income families. Further, MTW allows public housing agencies (1) exemptions from existing public housing and voucher rules and (2) more flexibility with how they use their Federal funds. This flexibility is authorized via exemptions of program requirements approved by HUD's Assistant Secretary that are identified in attachments C and D of the public housing agencies' MTW agreement. To use an exemption, the public housing agencies identify the specific authorized exemption in any of their annual plans.

During our preliminary review, we determined that the Authority's RAD conversion activities were generally completed in compliance with HUD's requirements; however, we noted some minor deficiencies that we communicated to HUD in a separate memorandum. Nevertheless, the focus of our review was the activities after the RAD conversion. Specifically, our audit objective was to determine whether the Authority complied with HUD's program requirements for conducting unit inspections and rent reasonableness determinations after the RAD conversion.

Results of Audit

Finding: The Authority Did Not Fully Comply With HUD's Requirements for Unit Inspections and Rent Reasonableness Determinations

The Authority did not fully comply with HUD's program requirements after its RAD conversion for conducting unit inspections and rent reasonableness determinations. Specifically, for all 206 units converted under RAD that the Authority owned, it did not obtain the services of a HUD-approved independent entity to perform unit inspections for compliance with HUD's housing quality standards[1] and rent reasonableness determinations. This condition occurred because the Authority initially did not realize that the independent entity inspections for housing quality standards and rent reasonableness determinations requirements remained applicable after the RAD conversion although the rents were set by HUD and the units were substantially rehabilitated. As a result, it inappropriately paid more than $394,000 in housing assistance payments and received more than $49,000 in administrative fees. Further, HUD and the Authority lacked assurance that the unit inspections and rent reasonableness determinations were properly conducted and HUD's and the tenant's interest was protected.

The Authority Did Not Fully Comply With HUD's Third-Party and Inspections Requirements For Unit Inspections

The Authority did not obtain the services of a HUD-approved independent entity to perform unit inspections for compliance with HUD's housing quality standards for any of the 206 units it owned for the period January 1, 2016, through August 5, 2016. HUD required at 24 CFR 983.59(b) that the Authority-owned units be inspected by an independent entity approved by HUD rather than the Authority. The Authority explained that four independent entities conducted inspections of the Authority-owned units. The entities included (1) City-County government's building inspection division, (2) housing finance agency for the Commonwealth of Kentucky, (3) equity investor for the RAD conversion, and (4) HUD inspector from the local field office. However, although the four entities were independent, we determined that three of the entities were not approved by HUD as required at 24 CFR 983.59(b) and the HUD inspector identified as the fourth entity conducted only a walk-through of a sampling of units.

In addition, the Authority's Executive Director stated that none of the inspections were specifically conducted for compliance with HUD's housing quality standards. Whereas, HUD's requirements at 24 CFR 983.156(a)(1) provided that housing agencies must inspect units to determine whether the housing rehabilitation has been completed in accordance with the housing

1 Housing quality standards are defined as the minimum quality standards for housing assisted under the Section 8 Housing Choice Voucher program. The Authority's public housing project was converted under RAD to the Section 8 Project-Based Voucher program. The Project-Based Voucher program required compliance with the same housing quality standards as the Housing Choice Voucher program.

assistance payments contract, including compliance with housing quality standards. Further, 24 CFR 983.103(c) required that the Authority not provide housing assistance on behalf of the family until the unit fully complied with HUD's housing quality standards. The purpose of the inspections conducted by the independent entities is listed below.

- The City-County government's building inspection division conducted inspections for the purpose of issuing certificate occupancies in order to allow any tenants to move-in.
- The Housing finance agency for the Commonwealth of Kentucky conducted inspections for the purpose of low-income housing tax credits identified in the RAD transaction.
- The equity investor for the RAD conversion conducted inspections for the purpose of its equity investment.
- HUD inspector from the local field office conducted a sampling walk-through of the units upon completion of the renovations.

Lastly, since the independent entities' inspections, the Authority's Chief Operating Officer stated that additional unit inspections conducted between the period January 1, 2016, and August 5, 2016, related to only if a move-out or eviction requiring an inspection for a new move-in or a special inspection.

The Authority explained that it initially did not realize that the independent entity inspections for housing quality standards requirements remained applicable after the RAD conversion although the units were substantially rehabilitated. However, as stated above, the Authority was required to obtain the services of HUD-approved independent entities to perform inspections on all 206 units owned by the Authority.

The Authority Did Not Fully Comply With HUD's Third-Party Requirements For Rent Determinations

The Authority obtained the services of an independent entity for determining the initial rent reasonableness for the 206 Authority-owned units; however, the independent entity was not approved by HUD. Specifically, 24 CFR 983.301(g) required that for Authority-owned units, the rent reasonableness be determined by an independent third-party approved by HUD. The Authority explained that it did not believe it was required to seek HUD's approval to use the independent entity because it was selected from a list of approved market analysts provided by the housing finance agency for the Commonwealth of Kentucky. We reviewed the list and determined that it did not show that the entity was approved by HUD for the purposes of Centre Meadows Apartments' initial rent reasonableness determination.

Further, the Authority failed to use an independent HUD-approved agency for rent reasonableness determinations occurring after the initial determinations. Specifically, 24 CFR 983.301(g) required that for Authority-owned units, the annual redetermination of rent be determined by an independent entity approved by HUD. The Authority explained that it did not realize that an independent entity was required to conduct the annual rent reasonableness determinations although the rents were set by HUD's RAD program. However, HUD's Office of Recapitalization explained that the rents provided by HUD are only the RAD portion of the rent analysis and it does not evaluate the rent reasonableness. Further, the RAD Notice 2012-32

REV-1 stated that notwithstanding HUD's calculation, initial Section 8 Project-Based Voucher program contract rents are subject to Section 8 Project-Based Voucher program requirements governing contract rents. To this effect, for all 206 Authority-owned units, the amount of the reasonable rent needed to be determined by an independent agency approved by HUD rather than by the Authority.

Nonetheless, the Authority obtained the services of an independent entity approved by HUD during our review. The Authority also provided documentation to support that the rents it previously approved were within the range of reasonable rents at the time of approval as determined by the independent entity.

Conclusion

The Authority initially did not realize that the independent entity inspections for housing quality standards and rent reasonableness determinations requirements remained applicable after the RAD conversion although the rents were set by HUD and the units were substantially rehabilitated. As a result, the Authority inappropriately paid $394,190 in housing assistance payments and received $49,014 in associated administrative fees. Further, HUD and the Authority lacked assurance that the unit inspections and rent reasonableness determinations were properly conducted and HUD and the tenants' interest was protected.

Recommendations

We recommend that the Director of HUD's Louisville, KY, Office of Public and Indian Housing require the Authority to

1A. Reimburse its Section 8 Project-Based Voucher program $443,204 ($394,190 in housing assistance payments and $49,014 in associated administrative fees) from nonproject funds for the payments related to the 206 Authority-owned units' inspections not conducted by a HUD-approved independent entity and for compliance with housing quality standards for the period January 1, 2016, through August 5, 2016.

1B. Ensure that HUD-approved independent third parties complete the unit inspections and determine the rent reasonableness for units it owns or seek an appropriate exemption of program requirements from the HUD Secretary.

1C. Ensure that in future RAD conversions, if any, unit inspections are conducted for compliance with HUD's housing quality standards after rehabilitation and construction is completed and before tenants move in.

1D. Provide adequate training to its staff to ensure compliance with Section 8 Project-Based Voucher program requirements for unit inspections and rent reasonableness determinations.

Scope and Methodology

We performed our onsite audit work between August 2017 and February 2018 at the Authority's office located at 300 West New Circle Road, Lexington, KY, and at our office in Atlanta, GA. The audit period was July 1, 2012, through July 31, 2017.

To accomplish our audit objective, we interviewed HUD program staff and the Authority's employees. In addition, we obtained and reviewed the following:

- Applicable laws; HUD's regulations at 24 CFR Parts 983 and 905; and Office of Public and Indian Housing Notice 2012-32, REV-1 and REV-2.

- The Authority's policies and procedures, RAD application, financing sources, construction draws, general ledgers, annual audited financial statements for fiscal years 2012 through 2016, executed written agreements, housing assistance payments contract, tenant files, and bank statements.

The universe consisted of 206 RAD-converted Section 8 Project-Based Voucher program units at Centre Meadows Apartments. The review considered 100 percent of the units for housing quality standards inspections. The review also considered each rent reasonableness determination completed during the scope. Further, we limited the questioned costs in the finding to August 5, 2016, because there was a HUD approval, dated August 5, 2016, through which the Authority expected to waive third-party requirements for unit inspections and rent reasonableness determinations under its MTW status.

Other Information

Computer-processed data generated by the Authority were not used to materially support our audit findings, conclusions, and recommendations. However, we did assess the reliability of the computer-processed data in the housing assistance payments register. Specifically, we used audit command language to complete a field verification and statistics query for the housing assistance payments register in Microsoft Excel. The tests detected no validity errors. Further, our conclusions were based on supporting documentation obtained during the audit, including but not limited to written agreements, tenant eligibility files, tenant relocation files, property site visits, expenditure support documents, and bank statements.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit 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.

- Relevance and reliability of information – Policies and procedures that management has implemented to reasonably ensure that operational and financial information used for decision making and reporting externally is relevant, reliable, and fairly disclosed in reports.

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that program implementation 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:

- The Authority did not comply with HUD's requirements for unit inspections and rent reasonableness determinations.

Appendixes

Appendix A

Schedule of Questioned Costs

Recommendation number	Ineligible 1/
1A	$443,204
Totals	**443,204**

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

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation | **Auditee Comments**

LEXINGTON-FAYETTE URBAN COUNTY HOUSING AUTHORITY
300 West New Circle Road • Lexington, KY 40505 • Phone: (859) 281-5060 • Fax: (859) 281-5055

Equal Housing Opportunity

June 21, 2018

Nikita Irons
Regional Inspector for Audit
Office of Inspector General, Office of Audit (Region 4)
75 Ted Turner SW, Room 330
Atlanta, GA 30303-3388

Re: Office of Inspector General (OIG) draft audit entitled "Lexington-Fayette Urban County Housing Authority, Lexington, KY: Rental Assistance Demonstration Section 8 Project-Based Voucher Program (the Draft Audit); comments of the Lexington-Fayette Urban County Housing Authority (LHA)

Dear Ms. Irons:

Thank you for the opportunity to submit comments regarding the Draft Audit on behalf of the LHA. Thank you also for modifications made to earlier draft materials.

The LHA has serious concerns regarding the Draft Audit. The LHA strongly objects to the Draft Audit's recommendation that the LHA reimburse funds to its voucher program, when the LHA proceeded in good faith, the housing produced was inspected multiple times and the housing's quality clearly has exceeded Housing Quality Standards (HQS).

Overall Context

Comment 1

I appreciate the Draft Audit's acknowledgements both that the LHA was recognized by HUD as having the first RAD transaction with a Federal Housing Administration (FHA) mortgage insurance for new construction or substantial rehabilitation and that the Authority's RAD conversion activities were generally completed in accordance with HUD's requirements. The latter statement is made in a footnote on page 5 of the Draft Audit, but should be featured much more prominently in any final audit to give the public a more accurate understanding of the audit's conclusions. Otherwise, OIG's final audit will be highly misleading.

Comment 2

The LHA's RAD project is an important, path-breaking success. HUD RAD staff strongly encouraged LHA's participation in the RAD program, and Pimlico/Centre Meadows was one of the first large-scale substantial rehabilitations of a family development to close under the RAD program. HUD's articulation of RAD program rules and its administrative process was at a relatively early stage. Yet, the project leveraged approximately $9.4 million in tax credit equity and LHA contributed approximately $9 million of LHA non-federal funds, to facilitate over $83,000 per unit in rehabilitation. The results are extremely positive for Lexington's current and future low-income households, LHA, HUD and the Lexington community.

visit our website at www.lexha.org

Ref to OIG Evaluation

Auditee Comments

Draft Audit Finding

Comment 3

The Draft Audit finds that after the RAD conversion, the Authority did not fully comply with HUD's requirements for third-party HQS inspections and rent reasonableness determinations. The LHA agrees that based on some misunderstandings regarding the applicability of program rules in the context of a substantial rehabilitation under RAD, for a relatively short time period after the units' completion, the steps it took did not adhere to the regulatory requirements in those respects. The LHA had these misunderstandings because in substance, the units far exceeded HQS and the contract rents set by RAD program rules clearly were reasonable.

Comment 4

With respect to HQS inspections, the Draft Audit acknowledges that four independent inspections took place on construction completion in addition to LHA staff inspections—by the City-County government's building inspection division, the state housing finance agency (HFA), the equity investor's inspector and a HUD inspector. The Draft Audit then attempts to denigrate these inspections' importance or relevance, however, by stating that the City-County's inspection was for purposes of issuing certificates of occupancy, the HFA inspections were "for the purpose of low-income housing tax credits", the equity investor conducted inspections "for the purpose of its equity investment" and the HUD inspector conducted a sampling walk-through of the units upon completion. The OIG's characterizations ignore that each inspector had important responsibilities to fulfill by the inspection and inspected to assure fulfillment of housing conditions standards: the City-County inspection to the Kentucky Building Code, the HFA and equity investor inspections to Internal Revenue Service standards for low-income tax credit units and the HUD inspections to standards needed to protect HUD in this FHA transaction. The equity inspector inspected with consideration among other standards to the Uniform Physical Condition Standard, a generally higher standard than HQS that HUD now is considering adopting for the voucher program, as well as to HQS. In view of these inspections and the units' level of rehabilitation, there is no substantive question that these units generally greatly exceeded HQS standards. Thus, the intent of the regulation was met.

Comment 5

Similarly, with regard to rent reasonableness, the rents set under RAD rules and reviewed by an independent entity selected from the HFA's approved market analysts clearly were within the reasonable range. The Draft Audit acknowledges that the LHA provided documentation to support that the rents it approved were within the range of reasonable rents at the time of approval as determined by the independent entity. That documentation indicated that the initial RAD rents, which have been increased only by Operating Cost Adjustment Factors, ranged from 93.1% of applicable fair market rents for 1-bedroom units to 82.7% for 3-bedroom units. The allowable reasonable rents for Centre Meadows' substantially rehabilitated units are considerably higher than those charged.

Ref to OIG Evaluation

Auditee Comments

Draft Audit Recommendations

Comment 4 and 6

The LHA strongly disagrees with recommendation 1A, that the LHA reimburse its Section 8 Project-Based Voucher program $394,190 in housing assistance payments and $49,014 in administrative fees, in connection with the variations from the regulations regarding inspections. Program recipients were housed in units that were inspected multiple times and clearly far exceeded HQS standards. In that sense there are no grounds to reimburse the Section 8 program; the Section 8 funds were used effectively for their authorized purpose, The LHA used approximately $9 million of LHA non-federal funds to produce that result -- units of outstanding quality despite the RAD-limited rental income to the project.

Comment 2, 4, and 6

The LHA acknowledges that LHA did not follow the letter of the inspections law; however, the intent of the law was met. Thus, it is unnecessary and counter-productive to set back affordable housing in Lexington by also requiring repayment of these funds to the program, in addition to the local funds that LHA already has expended. The Centre Meadows/Pimlico project is a good example of the important affordable housing uses to which LHA's non-federal funds have been put. To require repayment in this situation is punitive and vindictive.

Comment 7

Comment 8

Comment 9

Recommendation 1B is that the LHA ensure that HUD-approved independent third parties complete the unit inspections and determine rent reasonableness for the units it owns or seek an appropriate exemption of program requirements from the HUD Secretary. The LHA already has obtained the necessary exemption through a HUD-approved activity as part of its Moving-to-Work (MTW) demonstration participation. The OIG is aware of this, and thus its determination to retain the recommendation in the Draft Audit raises a question regarding its intent. Recommendation 1C is that the field office ensures in any future RAD conversions that HQS inspections are conducted as required. The LHA has no plans at this point for future RAD conversions, but will assure that the HQS inspections are done when required if any further RAD conversions are undertaken. Recommendation 1D is that the field office ensures that LHA provide adequate training to its staff to ensure compliance with Section 8 Project-Based Voucher program requirements for unit inspections and rent reasonableness determinations. The staff's involvement with the Draft Audit process should ensure that misunderstandings identified in the Draft Audit do not happen again, and in any event LHA's MTW approvals relieve LHA of the third-party inspection and rent reasonableness requirements for PHA-owned units.

Please reconsider the Draft Audit based on these comments. Thank you.

Sincerely,

Austin Simms
Executive Director

OIG Evaluation of Auditee Comments

Comment 1 The Authority stated that information presented in footnote on page 5 should be much more prominently featured to give the public a more accurate understanding of the audit's conclusions.

We agree with the Authority; therefore, we moved the information from its placement in a footnote on page 5 to page 4 of the report. Further, to give the public an accurate understanding, we added additional information also on page 4 to disclose the focus of our review.

Comment 2 The Authority stated that its project converted under the Rental Assistance Demonstration Program (RAD) leveraged $9.4 million in tax credit equity and the Authority contributed $9 million of its own non-Federal funds to facilitate over $83,000 per unit in rehabilitation.

As stated in the Background section of the report, the purpose of the RAD conversion was to preserve and improve properties including deferred maintenance by enabling public housing agencies to use private debt and equity to address immediate and long-term capital needs. Among other funds, expending of its own non-Federal funds was the route the Authority chose to address its rehabilitation needs as part of its RAD conversion.

Comment 3 The Authority stated that it agreed that it did not adhere to the regulatory requirements for a relatively short time period after the units' completion.

We appreciate the Authority's acknowledgement. However, the timeframe being short did not negate the requirement to ensure that the units met housing quality standards as defined by HUD prior to the tenants moving into the units. Further, the timeframe was short based on when the housing assistance payments started on January 1, 2016, through August 5, 2016, only due to the Authority seeking a waiver of the requirements as part of its Moving-To-Work (MTW) demonstration participation.

Comment 4 The Authority stated that the audit report ignored that each of the four inspectors had important responsibilities to fulfill with its inspections as it related to housing condition standards. In addition, the Authority stated that because of these inspections and the level of rehabilitation of the units, the intent of the regulation was met.

The audit report provided the specific purpose of the inspections conducted by the four inspectors. As stated in the finding, the Authority was required to obtain the services of an independent HUD-approved entity per 24 CFR 983.301(g) to conduct unit inspections for compliance with housing quality standards as defined by HUD. The Authority should work with HUD during the audit resolution process to address the finding and implement the recommendations.

Comment 5 The Authority stated that it demonstrated to us that rents it approved were within the range of reasonable rents at the time of approval as determined by the independent entity.

As stated in the finding, the Authority obtained the services of an independent entity approved by HUD during our review. The Authority also provided documentation to support that the rents it previously approved were within the range of reasonable rents at the time of approval as determined by the independent entity. However, prior to the audit, HUD and the Authority lacked assurance that the rents were reasonable at the time of approval.

Comment 6 The Authority disagreed to reimbursing its program per recommendation 1A and stated that it is counterproductive to set back affordable housing in Lexington, KY by also requiring repayment of these funds to the program, in addition to the local funds that the Authority has already expended.

Recommendation 1A addresses the deficiency and is made to ensure that the taxpayers' funds are spent in accordance with HUD's requirements, discussed in comment 4 above. In addition, expending of the local funds was the route the Authority chose to address its rehabilitation needs as part of its RAD conversion as discussed in comment 2 above. The Authority should work with HUD during the audit resolution process to address the finding and implement recommendation 1A.

Comment 7 Regarding Recommendation 1B to ensure that HUD-approved independent third parties complete the unit inspections and rent reasonableness for units owned by the Authority or to seek an appropriate exemption of program requirements from the HUD Secretary, the Authority stated that although we were aware of its exemption, we continued to keep the recommendation. Nonetheless, the Authority stated that it has already obtained the necessary exemption through a HUD-approved activity as part of its MTW demonstration participation.

We previously acknowledged in the Scope and Methodology section of the report that there was a HUD approval, dated August 5, 2016, through which the Authority expected to waive third-party requirements for unit inspections and rent reasonableness determinations under its MTW status. However, the Authority should work with HUD during the audit resolution process to ensure that recommendation 1B is fully addressed and implemented.

Comment 8 On recommendation 1C to ensure that housing quality standards inspections are conducted in any future RAD conversions, the Authority stated that it has no plans at this point for future RAD conversions, but will assure that the housing quality standards inspections are done when required if any further RAD conversions are undertaken.

We commend the Authority's willingness to ensure that HUD's requirements are met in future RAD conversions, if any. The Authority should work with HUD during the audit resolution process to fully implement recommendation 1C.

Comment 9 Concerning recommendation 1D to provide adequate training to its staff to ensure compliance with the Section 8 Project-Based Voucher program requirements for unit inspections and rent reasonableness determinations, the Authority stated that its staff's involvement with the audit process should ensure that misunderstandings identified in the report do not happen again.

We appreciate the Authority's staff's cooperation with our audit process and acknowledge that their experience with the audit may help ensure that program requirements are fully met moving forward. However, the Authority should work with HUD during the audit resolution process to fully implement recommendation 1D.