Issue Date June 1, 2012
Audit Report Number 2012-AT-1012

TO: Michael A Williams, Director, Greensboro, NC, Office of Public Housing, 4FPH

//signed//

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

SUBJECT: The Housing Authority of the City of Hickory, NC, Mismanaged Some of Its HUD Funds

HIGHLIGHTS

What We Audited and Why

We audited the public housing program of the Housing Authority of the City of Hickory, NC, due to a citizen's hotline complaint. Our objectives were to evaluate the merits of the complaint allegations and determine whether the Authority complied with U.S. Department of Housing and Urban Development (HUD) requirements for procurement, cash disbursements, a 2004 Resident Opportunity and Self-Sufficiency (ROSS) grant, and inventory control.

What We Found

The Authority failed to administer some of its HUD funds in accordance with requirements. It awarded contracts to family members, disbursed funds for ineligible purchases, failed to comply with the financial requirements of its ROSS grant, and failed to maintain an adequate inventory system. These deficiencies generally occurred because management failed to maintain adequate internal controls.

The Authority awarded four contracts to family members in violation of conflict-of-interest requirements. This violation occurred because the Authority's board and executive director failed to follow provisions of its consolidated annual contributions contract and procurement policy prohibiting contracting with family members. As a result, the Authority expended $522,125 for ineligible contracts and risked losing the public's confidence in the integrity of its operations.

The Authority lacked adequate controls over its cash disbursements. It improperly charged expenses to its Public Housing Capital Fund program and could not support compliance with its procurement policy for some disbursements. These deficiencies occurred because the Authority did not have sufficient written procedures and its staff was not fully aware of some program requirements. As a result, the Authority expended $8,881 for ineligible purposes and $10,811 for unsupported purchases.

The Authority also mismanaged its ROSS program established to help residents gain economic sufficiency and failed to maintain an adequate inventory control system. As a result, it could not assure HUD that it used $69,823 for eligible ROSS grant expenses, or that funds it expended for equipment and supplies were properly used for Authority activities.

What We Recommend

We recommend that the Director of the Greensboro Office of Public Housing require the Authority to (1) reimburse its public housing operating fund $522,125 using non-Federal funds for conflict-of-interest contracts; (2) provide assurance that its board and management understand their roles and responsibilities regarding real or apparent conflicts of interest; (3) develop, implement, and enforce adequate written procedures for its cash disbursement function and ensure that responsible staff is trained; (4) require the Authority to provide support showing that $69,823 in ROSS grant funds was used for eligible grant expenses and repay any grant funds determined to be ineligible; and (5) develop and implement an improved inventory control system.

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

Auditee's Response

We discussed the findings with Authority officials during the audit. We provided a copy of the draft report to the Authority on April 9, 2012, for its comments and discussed the report with Authority officials at an exit conference on April 18,

2012. The Authority provided its written comments to our draft report on April 30, 2012. The Authority generally agreed with the contents of the report.

The complete text of the Authority's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Housing Authority of the City of Hickory was established in 1966 pursuant to the Housing Authorities Law of the State of North Carolina to address a severe shortage of decent, safe, and sanitary housing that could be afforded by persons of moderate income. The Authority's governing body is a seven-member board of commissioners appointed by the mayor. An executive director is responsible for daily operations.

The Authority manages 311 conventional low-income public housing units and 449 Housing Choice Voucher program units. It has implemented project based budgeting and accounting under HUD's asset management program. The Authority annually receives funds from the U.S. Department of Housing and Urban Development (HUD) to operate its programs and maintain its housing stock. It also received a $250,000 Resident Opportunity and Self-Sufficiency (ROSS) grant during 2004, which was still active during our audit period. The grant was designed to provide expanded educational opportunities, job training, technology training and access, and other programs to help public housing residents achieve self-sufficiency.

We performed the review after we received an anonymous citizen hotline complaint containing many allegations, including questionable payments to individuals and vendors, personal use of Authority vehicles and credit cards, inappropriate transfers of funds between Authority accounts, conflicts of interest and nepotism, excessive maintenance purchases, and falsification of maintenance work orders. Review of the complaint is detailed in the Scope and Methodology section.

Our objectives were to evaluate the merits of the complaint allegations and determine whether the Authority complied with U.S. Department of Housing and Urban Development (HUD) requirements for procurement, cash disbursements, a 2004 ROSS grant, and inventory control.

RESULTS OF AUDIT

Finding 1: The Authority Violated Conflict-of-Interest Requirements

The Authority awarded contracts to family members in violation of conflict-of-interest requirements. This violation occurred because the Authority's board and executive director failed to follow provisions of its consolidated annual contributions contract[1] and its procurement policy prohibiting contracts with family members. As a result, the Authority expended $522,125 for the ineligible contracts and risked losing the public's confidence in the integrity of its operations.

The Authority Awarded Contracts to Family Members

We reviewed 12 procurement actions valued at $1.57 million out of a universe of 45 procurements valued at $2.1 million executed during our audit period. With the exception of those actions discussed in finding 2, most contracts appeared to have been properly procured or contained only minor deficiencies. However, the Authority awarded three contracts to a board member's brother and obtained services from the executive director's husband in violation of the conflict-of-interest provisions in its consolidated annual contributions contract and its procurement policy.

During 2008, the Authority awarded three contracts to a maintenance company owned by the brother of a board member. Two contracts were for building maintenance services, and the other was to replace exterior doors. The executive director and the board knew of the relationship but did not believe that there was a conflict of interest, since the board member did not vote when the board selected his brother's company. Since the consolidated annual contributions contract and the Authority's procurement policy specifically prohibited contracting with family members, the Authority was clearly in violation of the conflict-of-interest requirements. The $519,390 paid to the maintenance company from HUD operating funds was an ineligible expense, and the Authority must repay it from non-Federal funds.

During 2009, the Authority entered into another conflict-of-interest contract when it purchased landscaping and maintenance services from the executive director's husband. The Authority paid that individual a total of $3,935 between May 2009 and March 2010. It paid $575 of the charges using non-Federal funds, and the

[1] A consolidated annual contributions contract is a written contract between HUD and a public housing authority in which the authority agrees to administer its public housing program in accordance with HUD regulations and requirements.

executive director repaid the Authority $625 from her personal funds. The Authority must repay the ineligible balance of $2,735 using non-Federal funds.

Contracting with family members of the board or staff could lessen the public's faith in the Authority's contracting integrity and discourage companies from competing for contracts, thus weakening its ability to obtain fair and reasonable prices. The Authority could have requested that HUD grant a waiver of the requirements, but it did not do so or otherwise notify HUD of the conflicts of interest.

Conclusion

The Authority spent $522,125 in HUD funds for ineligible purposes because it failed to follow the provisions prohibiting conflicts of interest contained in both its consolidated annual contributions contract and its procurement policy. This failure will result in the Authority's being required to repay the funds and could also result in a loss of public confidence in the integrity of its operations.

Recommendations

We recommend that the Director of HUD's Greensboro, NC, Office of Public Housing

1A. Require the Authority to reimburse its public housing operating fund $522,125 using non-Federal funds.

1B. Require the Authority to provide assurance that its board and management understand their roles and responsibilities regarding real or apparent conflicts of interest.

Finding 2: The Authority Lacked Adequate Controls Over Its Cash Disbursements

The Authority lacked adequate controls over its cash disbursements. It improperly charged expenses to its Public Housing Capital Fund program and could not support compliance with its procurement policy for some disbursements. These deficiencies occurred because the Authority did not have sufficient written procedures and its staff was not fully aware of some program requirements. As a result, the Authority expended $8,881 for ineligible purposes and $10,811 for unsupported purchases.

The Authority Lacked Adequate Controls Over Its Cash Disbursements

We reviewed a sample of 21 checks totaling $40,548 from a universe of 732 checks issued during 4 randomly selected months to determine whether expenses were eligible, reasonable, and supported. The Authority spent $19,692 for ineligible or unsupported costs. It did not have written procedures for employees to follow for some of its basic finance functions, and the employees were not always aware of the applicable HUD or Authority requirements.

Ineligible Expenses

Authority staff incorrectly charged $8,881 to the Authority's 2008 and 2009 Capital Fund programs' management improvement budget line item. The regulations (24 CFR (Code of Federal Regulations) 968.112 (g)) allowed for management improvements that were development specific or Authority wide in nature. Examples of allowable expense items would include expenditures for upgrading the operation of the Authority's developments, sustaining physical improvements at its developments, or correcting management deficiencies. Some of the Authority's disbursements did not comply with the requirements. Ineligible expenditures included summer camps, field trips, sports uniforms, and back-to-school events for organizations that some Authority residents attended.

We reviewed the Authority's monthly cell phone statements and found that an employee used the assigned phone for personal use, resulting in improper charges of $364 during 1 month. The Authority repaid the improper charges from non-Federal funds during our onsite work. The incident occurred because the phone bill had not been properly reviewed.

Unsupported Costs

The Authority did not maintain documentation to support that it had properly procured six purchases totaling $10,811. It was required by its procurement policy to obtain a reasonable number of quotes (preferably three) for small purchases exceeding $2,000. Although Authority staff members said that the quotes were obtained, they could not provide supporting documentation.

Authority Fuel Cards
We reviewed the Authority's fuel card statements between May and September of 2011 to determine whether the charges were allowable and properly supported. The Authority lacked adequate controls over fuel card purchases. It had asked its employees to submit initialed receipts to its finance manager and document the vehicle mileage after each use of the fuel card but maintained no written policy or procedures governing the use of the cards. While some fuel purchases appeared excessive, we were unable to determine whether they were reasonable because the employees did not consistently follow the instruction to record the vehicle mileage and multiple employees sometimes shared the same fuel card.

Conclusion

Authority management had not implemented sufficient controls to ensure that cash disbursements were made in accordance with HUD's requirements. As a result, the Authority expended $8,881 for ineligible purposes and $10,811 for unsupported purchases. The Authority must implement effective controls to ensure that future purchases are eligible, reasonable, and fully supported.

Recommendations

We recommend that the Director of HUD's Greensboro, NC, Office of Public Housing require the Authority to

2A. Develop, implement, and enforce adequate written procedures for its cash disbursement function.

2B. Ensure that the appropriate staff members are trained regarding the requirements for capital fund, procurement, and other cash disbursements.

2C. Repay $8,030 to the U.S. Treasury using non-Federal funds for the ineligible expenses charged to the closed 2008 Capital Fund grant.

2D. Provide $851 in eligible expenses for the open 2009 Capital Fund grant or reimburse the grant using non-Federal funds.

2E. Provide documentation supporting that $10,811 in purchases charged to the operating accounts were properly procured. The Authority should repay any costs found to be ineligible to the appropriate public housing operating account(s).

Finding 3: The Authority Mismanaged Its ROSS Program

The Authority mismanaged its ROSS program established to help residents gain economic sufficiency. The Authority failed to comply with the grant's financial requirements because management did not understand some requirements. As a result, the Authority could not assure HUD that it used $69,823 for eligible grant expenses.

The Authority Failed To Comply With the Grant Agreement

HUD awarded the Authority a $250,000 3-year ROSS program grant during fiscal year 2004 and extended it through 2011. The intent of the program was to help public housing residents achieve self-sufficiency through expanded educational opportunities, job training, technology training and access, and other programs. The Authority entered into memorandums of understanding with nine subrecipients to provide these services.

We reviewed the Authority's program implementation through the sub-recipients and found that management had failed to comply with the grant agreement's financial requirements.

The Authority drew down grant funds through HUD's Line of Credit Control System as needed. We reviewed 8 of the 32 drawdowns from the initial period and the 9 drawdowns (as one lump sum) from the grant extension and found that the Authority could not support that it used $69,823 of the $103,109 (68 percent) reviewed for eligible activities. Of the $69,823, the Authority drew down $66,900 before its sub-recipients incurred costs, a violation of the grant agreement. Additionally, the Authority did not maintain complete accounting records, such as a general ledger, showing the sources and uses of grant funds as required by 24 CFR 85.20(b)(2).

Authority management failed to ensure compliance with the grant agreement because it was not aware of the grant's financial requirements. The executive director stated that she was not aware that the Authority could draw down grant funds only for costs already incurred. Instead, she drew down funds to pay advances to the sub-recipients and did not require them to provide supporting receipts showing how they used the funds. She also failed to retain accounting records of grant transactions before 2009 when the Authority changed accounting systems.

Conclusion

The Authority mismanaged its ROSS program because management failed to understand all of the program requirements. It must provide HUD proper support showing that the funds were used for the program's intended purpose or repay the funds.

Recommendations

We recommend that the Director of HUD's Greensboro, NC, Office of Public Housing

3A. Require the Authority to provide support showing that the $69,823 in grant funds was used for eligible grant expenses. Any grant funds determined to be ineligible should be repaid to the U.S. Treasury using non-Federal funds.

3B. Review the remaining $142,272 in grant funds to determine whether they were expended in accordance with Federal regulations and grant requirements. Require the Authority to repay any funds determined to be ineligible to the U.S. Treasury using non-Federal funds[2].

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[2] The Authority expended $245,382 of the $250,000 ROSS grant. Of the $245,382 spent, we reviewed $103,109 during our audit and are asking HUD to review the remaining $142,272. The remaining $4,618 (250,000-245,382) is being recaptured by HUD.

Finding 4: The Authority Failed To Maintain an Adequate Inventory Control System

The Authority did not maintain an adequate inventory control system. Management had not implemented written procedures for staff to follow, and the Authority's informal system was inadequate. As a result, the Authority could not assure HUD that funds expended for equipment and supplies were properly used for Authority activities or that the values reflected on its inventory records were accurate.

The Authority Lacked Inventory Control Procedures

The Authority did not follow HUD's requirements for inventory. The regulations at 24 CFR Part 85 required the Authority to maintain effective control and accountability over all assets and keep detailed property records.

The Authority's inventory controls were not fully written and did not comply with HUD's requirements. Its cash management control policy required that an inventory system be established and maintained, but management had not developed written procedures for staff to follow. This deficiency caused staff to rely on unwritten procedures that were not consistently effective. One Authority staff member described the process as trial and error. In addition, the Authority did not have policies or procedures for conducting periodic physical inventories or making inventory adjustments. The building services manager claimed to have performed an annual physical inventory, and some staff members confirmed their input to an annual inventory. However, the Authority was not able to provide documentation to show that all Authority assets were inventoried or that inventory adjustments submitted by staff had been made.

The Authority's inventory records contained errors and omissions. Review of the inventory listing showed many deficiencies such as incorrect or missing equipment purchase or installation dates and missing bar codes, serial numbers, or both. In addition, equipment disposition dates were not always recorded, and the inventory was not updated on a timely basis for installations.

In an attempt to locate six recently purchased refrigerators, we asked Authority staff to provide their locations. Staff first provided incorrect locations, and it took several employees about a week to provide the correct locations. The work orders provided to show installation of the new refrigerators were not accurate or were incomplete. One work order incorrectly showed that the old refrigerator had been replaced with a used one, not the newly purchased refrigerator. Another showed that the existing refrigerator had been repaired and did not mention installing a new one. None of the work orders included serial numbers for properly entering the new refrigerators into the inventory system so that they could be easily located.

The inventory storage areas were often unsecured and appeared to be in disarray. During the review, the executive director took action to improve the physical security of the inventory storage areas. She also acknowledged that staff had not properly completed work orders or signed out supplies and promised to take additional measures to improve the system.

Conclusion

The Authority must document and implement an improved inventory control system including procedures for conducting and documenting periodic physical inventory counts and adjusting the asset records. After the Authority makes these needed improvements, it will be able to more reliably demonstrate what assets it has and their correct locations and account for any assets which may have been lost, stolen, or disposed of due to their condition. It will also be able to better assure HUD that funds expended for equipment and supplies were properly used for Authority activities and that the values reflected on its inventory records are accurate.

Recommendations

We recommend that the Director of HUD's Greensboro, NC, Office of Public Housing require the Authority to

4A. Develop and implement an improved inventory control system, including procedures for conducting and documenting periodic physical inventory counts and adjusting its asset records.

4B. Perform a complete physical inventory and make the necessary accounting system adjustments.

SCOPE AND METHODOLOGY

Our objectives were to evaluate the merits of the complainant's allegations and determine whether the Authority complied with HUD's requirements for procurement, cash disbursements, a 2004 ROSS grant, and inventory control.

Our primary objective was to evaluate the allegations in the complaint. The complainant alleged that (1) questionable payments had been made to individuals and vendors, (2) payments were made to an individual before being hired, (3) staff members were using Authority vehicles and credit cards for personal use, (4) there were many questionable fund transfers, (5) conflicts of interest and nepotism existed, (6) there were excessive maintenance purchases, and (7) staff had falsified work orders. Several other allegations appeared to be subjective or outside HUD's purview, and we did not evaluate those.

Although the complaint often lacked needed specificity, we were successful in verifying the existence of questionable payments (findings 1, 2, and 3) and that conflicts of interest existed (finding 1). However, we determined that the alleged improper payment made to an individual before being hired was false (non-Federal funds were used). We were also unable to confirm that staff members were using Authority vehicles or credit cards for personal use, whether maintenance purchases were excessive, or whether staff had falsified work orders. We did audit work in all of these areas, but the allegations were not specific, and our samples did not show anything improper. However, the internal control weaknesses identified throughout this report could result in such deficiencies, and our sample results only pertained to the items sampled and not the entire universe of transactions. As a result of our work on the complaint, we elected to expand our objectives to determine whether procurements, cash disbursements, the 2004 Ross grant, and inventory control were being accomplished in accordance with HUD's requirements.

To accomplish our objectives, we reviewed

- Financial management regulations at 24 CFR 85.20, HUD's applicable annual contributions contracts with the Authority, procurement regulations at 24 CFR 85.36, monitoring regulations at 24 CFR 85.40, and HUD's Greensboro, NC, Office of Public Housing files pertaining to the Authority.

- The Authority's policies and procurement manuals, 12 procurement actions, maintenance logs, fund transfers, ROSS grant draw requests, Authority credit card and bank statements, the two latest Authority audits, and the Authority's organizational chart.

We interviewed the complainant, Authority employees, and HUD's Greensboro, NC, public housing staff involved with oversight of the Authority's programs. We selected several non-statistical samples as described below. The results from these samples pertain only to the items sampled and were not projected to the universe as a whole.

We reviewed 12 procurement actions valued at $1.57 million out of a universe of 45 procurements valued at $2.1 million executed during our audit period. We began with a non-statistical sample of 5 procurement actions from a universe of 39 occurring during the audit period. We selected these five contracts to ensure that the sample included small purchases, a purchase that was approved by the board, and a purchase from each year of our audit period. Seven of the 21 checks we selected for disbursement testing (described below) represented purchases covered by the Authority's procurement policy. We added these 7 to the original sample of 5 to arrive at the sample of 12 procurement actions. We reviewed all 12 for compliance with the Authority's procurement policy and HUD's requirements.

We selected a non-statistical sample of 21 checks totaling $40,548 out of a universe of 732 checks totaling $682,616 to determine whether costs were eligible, reasonable, and supported. We selected 4 months of disbursements for inclusion in our universe, which ensured that each fiscal year of our audit period was represented. We selected 12 checks totaling $35,610 that were over $1,500 and did not appear to be a part of the normal course of Authority business. The remaining nine checks totaling $4,938 were selected based on the payee or the amount paid (payee with same last name as Authority employees or purchases with unusually high dollar amounts).

The Authority completed 41 Line of Credit Control System drawdowns totaling $245,382 for its 2004 ROSS grant: 32 drawdowns from the initial 36-month grant and 9 drawdowns from a 6-month extension. We selected a non-statistical random sample of 8 (25 percent of the universe) drawdowns totaling $50,209 out of a universe of 32 drawdowns totaling $192,482 to determine whether the drawdowns had adequate support and were made in accordance with the grant agreement. Additionally, the drawdowns totaling $52,900 completed during the extension were reviewed as a lump sum and counted as sample item number 9.

We reviewed 100 percent of the Authority's gasoline card statements from May through September 2011 to determine whether the charges were allowable and properly supported.

We performed our onsite work from August 24, 2011, through January 26, 2012, at the Authority's office at 841 South Center Street, Hickory, NC. The audit covered the period January 2009 through July 2011 and was extended as necessary.

We tested all electronic data as we performed our audit steps. We did not rely on any supplied data without tracing it to source documentation.

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 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 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 objectives:

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

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and obligations.

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 Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The Authority violated conflict-of-interest requirements (see finding 1).
- The Authority lacked adequate controls over its cash disbursements (see finding 2).
- The Authority mismanaged its ROSS program (see finding 3).
- The Authority failed to maintain an adequate inventory control system (see finding 4).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/	Unsupported 2/
1A	$522,125	
2C	8,030	
2D	851	
2E		$10,811
3A		69,823
Total	$531,006	$80,634

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

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

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

April 30, 2012

James D. McKay
Regional Inspector General for Audit
U. S. Department of Housing and Urban Development
Office of Audit, Box 42
Richard B. Russell Federal Building
75 Spring Street, SW, Room 330
Atlanta, Georgia 30303-3388

Dear Mr. McKay:

This is in reply to your April 11, 2012 letter enclosing a draft report of the Housing Authority of Hickory, NC for our review. The draft report provides four findings and recommendations and requested that the Authority review those findings and provide your office with our comments. You encouraged us to provide alternative resolutions.

Thank you for the opportunity to review and comment on your draft report. First, both the Board of Commissioners and I wish to assure the U. S. Department of Housing and Urban Development (HUD) that it is now and has always been the intent of this agency to operate its programs in full compliance with all applicable statutory, regulatory and other program requirements. We also wish to assure HUD that we take the issues raised in the draft report very seriously and fully intent to cooperate with HUD make all necessary corrections and resolve issues raised as expeditiously as possible.

As requested, enclosed are our comments on the draft report. If you have any questions, please do not hesitate to contact me.

Sincerely,

Alanda Jackson
Executive Director

CC: Michael Williams- Greensboro HUD Office
Enclosures

Finding 1. The Authority Violated Conflict-of-Interest Requirements

OIG Finding.

The Authority awarded contracts to family members in violation of the conflict-of-interest requirements. This violation occurred because the Authority's board and executive director failed to follow provisions of its consolidated annual contributions contract and its procurement policy prohibiting contracts with family members. As a result, the Authority expended $522,125 for ineligible contracts and risked losing the public's confidence in the integrity of its operations.

OIG Recommendation.

1A. Require the Authority to reimburse its public housing operating fund $522,125 using non-Federal Funds.

1.B. Require the Authority to provide assurances that its board and management understand their roles and responsibilities regarding real and apparent conflicts of interest.

HACH Response.

Recommendation 1A.

Comment 1

The HACH acknowledges and regrets the lapse in compliance with the conflict-of-interest requirements and is committed to the correction of the lapse. The HACH would like to point out that the lapse occurred not because of any willful attempt to circumvent the requirements, but a misunderstanding of those requirements. It assumed that recusal by the affected Board Member would address the conflict of interest. We now realize that recusal is not sufficient and will be more diligent in the future.

While HACH acknowledges its error, it believes that the requirement to reimburse its public housing operating fund $522,125 is not the appropriate or only remedy to the noncompliance. Moreover, given the recent past Congressional appropriations for the public housing program and the HACH's current balance of non-Federal funds, the HACH believes that alternative actions would be more effective and financially prudent for the

HACH and its residents. In considering alternative corrective actions, HACH believes that consideration should be given to the entire body of facts as it relates to the HACH and this matter.

First, it should be noted that the HACH has historically been a High Performer under HUD's Public Housing Assessment Program (PHAS). HUD recently made significant revisions to the PHAS scoring and the HACH's score under the new rating system dropped to 86 points out a possible total of 100 points, only 4 points from High Performer status. Having adjusted its operations based on the new indicators, HACH anticipates being once again designated as a High Performer under PHAS.

Second, we note that the OIG indicates that it reviewed $1.57 million out a universe of $2.1 million executed during the audit period. The OIG review comprised almost 75 per cent of the procurements during the period. The OIG states "most of the contracts appeared to have been properly procured or contained only minor deficiencies".

Third, the HACH did not use the funds in question for frivolous and otherwise ineligible work items. In fact, the OIG noted that the contracts cited provided maintenance related services to HACH public housing and benefited it residents. Under ordinary circumstances such services would be eligible expenses under the Operating Fund. As such, the public housing program received a substantial benefit from the services provided under those contracts. To require the HACH to repay the entire $522,125 under these circumstances serves no practical benefit to either the Federal government, the tax payers or the HACH residents. Instead, it would constitute an unjust enrichment to the public housing program and adversely affect the ability of the HACH to provide services to its residents given the reduced current level of appropriations by Congress for our programs.

As noted above, the HACH argues that repayment is not the only remedy in cases of noncompliance. While the Operating Fund regulations at 24 CFR 990 do not address program deficiencies, the Comprehensive Grant Program which has since become the Capital Fund does and provides an applicable and appropriate precedent. Specifically, 24 CFR 968.330(c) - PHA Performance and Evaluation Report provides that "HUD shall design corrective action to prevent a continuation of the deficiency, mitigate any adverse effects of the deficiency to the extent possible, or prevent recurrence of the same or similar deficiencies; ". 24 CFR 968(d) goes on to list up 8 possible corrective actions including "Take such other corrective actions HUD determines is appropriate to correct the deficiency." It is clear that HUD recognizes that in the public housing program there are other alternatives to addressing program deficiencies other than simply to repay funds.

In view of the above, the HACH recommends that the appropriate corrective action in this case would be, as discussed below, for all levels of the HACH to receive training regarding the ethics requirements of both the ACC and 24 CFR 85.36. In addition, the HUD Greensboro Office now requires the HACH to submit all procurements to its office for pre-award approval. We assume that the HUD Greensboro Office will continue this practice until it is assured that the HACH understands and is complying with these requirements. The HACH believes that these are more appropriate actions than repaying this significant sum from limited and scarce resources and will achieve the ultimate goal of continual long term compliance.

Recommendation 1B.

Comment 5

The HACH Executive Director, Board of Commissioners and outside Counsel have met and discussed the conflict of interest requirements and now fully understand those requirements. In addition, the HACH Executive Director, Board of Commissioners and HACH staff will all receive supplemental training on the ethics requirements of the ACC and HUD regulations at 24 CFR 85.36.

Finding 2. The Authority Lacked Adequate Controls Over its Cash Disbursements

OIG Finding.

The Authority lacked adequate controls over its cash disbursements. It improperly charged expenses to its Public Housing Capital Fund program and could not support compliance with its procurement policy for some disbursements. These deficiencies occurred because the Authority did not have sufficient written procedures and its staff was not fully aware of some program requirements. As a result, the Authority expended $8,881 for ineligible purposes and $10,811 for unsupported purchases.

OIG Recommendation.

2A. Develop, implement, and enforce adequate written procedures for cash disbursement function.

2.B. Ensure that the appropriate staff members are trained regarding the requirements of the capital fund, procurement and other cash disbursements.

2C. Repay $8,030 to the U.S. Treasury using non-Federal funds for ineligible expenditures charged the close 2008 Capital Fund grant.

2D. Provide $851 in eligible expenses for the open 2009 Capital Fund grant or reimburse the grant using non-Federal funds.

2E. Provide documentation supporting that the $10,811 in purchases charged to the operating accounts were properly procured. The Authority should repay any costs found to be ineligible to appropriate public housing operating accounts(s).

Comment 5

Recommendation 2A and 2B..

The HACH agrees and will develop the written procedures and obtain the required training. The HACH staff attended procurement training at the HUD Greensboro Office in March, 2012. The appropriate HACH staff is scheduled to attend financial management training from May 14 - 18, 2012 through the HUD Greensboro Office.

Recommendation 2C and 2D.

Comment 2

The HACH disagrees with the Finding regarding Capital Fund Management Improvements. The OIG Audit did not cite 24 CFR 968.112(g) in its entirety and omitted pertinent eligibility language. Specifically, 24 CFR 968.221(g)(2)(i) General Management Improvement costs reads as follows:

> (i) Eligible costs include general management improvement costs, such as: management, financial, and accounting control systems of the PHA; adequacy and qualifications of PHA personnel, including training; <u>resident programs and services through the coordination of the provision of social services from tribal or local government or other public and private entities</u>: resident and development security; resident selection and eviction; occupancy; rent collection; maintenance; and equal opportunity.(emphasis added).

The OIG cited ineligible expenditures to include: summer camps, field trips, sports uniforms, and back to school events for organizations that some Authority residents attended. All of the OIG cited expenditures were for "resident programs and services" authorized under 24 968.112(g)(2)(i).

Recommendation 2E.

Comment 3

The requested documentation will be sent under separate cover later this week.

Finding 3. The Authority Mismanaged Its ROSS Grant.

OIG Finding.

The Authority mismanaged its ROSS program established to help residents gain economic sufficiency. The Authority failed to comply with the grant's financial requirements because management did not understand some requirements. As a result, the Authority could not assure HUD that it used $69,823 for eligible grant expenses.

OIG Recommendation.

3A. Require the Authority to provide support showing that the $69,823 in grant funds was used for eligible grant expenses. Any grant funds determined to be ineligible should be repaid to the U.S. Treasury using non-Federal funds.

3.B. Review the remaining $142,272 in grant funds to determine whether they were expended in accordance with Federal regulations and grant requirements. Require the Authority to repay any funds determined to be ineligible to the U.S. Treasury using non-Federal Funds. Ensure that the appropriate staff members are trained regarding the requirements of the capital fund, procurement and other cash disbursements.

HACH Response.

Comment 4

Recommendation 3A.

The requested documentation will be sent under separate cover later this week.

Recommendation 3B.

This recommendation is directed toward the HUD Greensboro Office. The HACH will cooperate fully with the HUD Greensboro Office to assist them in their review.

Comment 5

Finding 4. The Authority Failed to Maintain an Adequate Inventory Control System.

OIG Finding.

The Authority did not maintain an adequate inventory control system. Management had not implemented written procedures for staff to follow, and the Authority's information system was inadequate. As a result, the Authority could not assure HUD that funds expended for equipment and supplies were properly used for Authority activities or that the values reflected on its inventory records were accurate.

OIG Recommendation.

4A. Develop and implement an improve inventory control system, including procedures for conducting and documenting periodic physical inventory counts and adjusting its asset records.

4.B. Perform a complete physical inventory and make the necessary account system adjustments.

HACH Response.

Recommendation 4A. HACH has contracted with Nelrod Company to develop a new inventory control system. A copy of the contract is attached. The HACH has already distributed a new draft of an inventory control system for their review and anticipates adopting a new system at its regularly scheduled meeting in May, 2012.

Recommendation 4B. HACH will complete a physical inventory and make the necessary accounting system adjustments by July 31, 2012. HACH will send a notification of completion to the HUD Greensboro Office at that time.

OIG Evaluation of Auditee Comments

Comment 1 The conflicts of interest which resulted in $522,125 of ineligible costs were serious violations of both the Authority's annual contribution contract and procurement policy. As such, we believe that repayment from non-Federal funds is the appropriate action. The language in the CFR states that HUD may direct the PHA to take one or more of the corrective actions in 24 CFR 968.335 (e). Note that the sixth corrective action is to reimburse, from non-federal sources, one or more program accounts for any amounts improperly expended.

Comment 2 Although we agree that 24 CFR 968.221 (g) (2) (i) states that the Authority can spend management improvement on resident programs and services, the Public and Indian Housing Comprehensive Improvement Assistance Handbook 7485.1 contains the complete definition for eligible expenditures. The Handbook states that eligible costs include hiring of additional staff to coordinate services as drug education, resident training, assistance to a resident management corporation, and economic development. The costs that we reported were ineligible did not fall within those parameters.

Comment 3 We did not receive the documentation the Authority promised to provide in order to show that $10,811 in purchases charged to the operating accounts were properly procured (Recommendation 2E). The Authority should provide the documentation to the HUD Greensboro field office in order to clear the recommendation.

Comment 4 The documentation provided by the Authority was not sufficient to support that $69,823 in grant funds was used for eligible grant expenses (Recommendation 3A). The Authority should provide complete documentation to the HUD Greensboro field office in order to clear the recommendation.

Comment 5 The Authority stated that it agrees with the findings and has taken or plans to take various actions to address deficiencies. Notably, the executive director and board of commissioners met with outside counsel to gain a full understanding of the conflict of interest requirements. It also plans supplemental ethics training for all Authority staff. Authority staff attended procurement training at the HUD Greensboro office and has additional financial management training scheduled. It employed a contractor to develop a new inventory control system and plans to complete a physical inventory and make the necessary accounting adjustments by July 31, 2012. We commend the Authority for timely addressing deficiencies cited in this report.