audit report

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TO: William Vasquez, Director, Los Angeles Office of Community Planning and Development, 9DD

Joan S. Hobbs

FROM: Joan S. Hobbs, Regional Inspector General for Audit, Region IX, 9DGA

SUBJECT: The City of Los Angeles Housing Department Did Not Adequately Monitor HOME Program-Assisted Rehabilitation Construction

HIGHLIGHTS

What We Audited and Why

We audited the City of Los Angeles Housing Department's (Department) single-family and small multifamily rehabilitation programs funded by the HOME Investment Partnerships Program (HOME program) as part of our annual audit plan. Our preliminary survey of the Department identified its housing rehabilitation activities under its Homeownership and Preservation Division to be at risk for waste, fraud, and abuse. The objectives of our audit were to determine whether, for single-family and small multifamily properties, the Department (1) effectively monitored construction bids, costs, and quality; (2) ensured that borrowers and properties met eligibility requirements for income and affordability; (3) properly reported HOME program activities to the U.S. Department of Housing and Urban Development (HUD); and (4) properly allocated soft costs between HOME program administrative accounts and direct activity cost accounts.

What We Found

The Department did not ensure that all HOME-assisted rehabilitation work on single-family and small multifamily properties met all applicable construction standards and/or was complete. We observed that $45,797 in HOME program funds assisted deficient or incomplete construction for three single-family rehabilitation activities monitored by the

Department. We also identified $421,828 in HOME funds that assisted single-family purchase-acquisition activities for which rehabilitation work was not completed as required. Finally, we observed rehabilitation construction deficiencies at five multifamily properties that one developer was allowed to rehabilitate without departmental monitoring. The developer received $793,775 for the five properties and more than $4.8 million for 35 properties we did not inspect. These problems stemmed from inadequate operating policies and procedures and a lack of quality control procedures regarding the construction monitoring function.

The Department had incomplete documentation of income eligibility and property values for 10 of 17 loan approval files we reviewed. This deficiency occurred because the Department had inadequate operating policies and procedures regarding its loan approval functions and did not adequately support claims of zero income for all adult household members.

Also, the Department did not report the status of its HOME program activities to HUD within the required timeframes. This deficiency occurred because the Department's databases and financial system were not integrated with HUD's Integrated Disbursement Information System, and the Department did not have manual data entry procedures in place to prevent and detect errors or delays.

What We Recommend

We recommend that HUD require the Department to develop, maintain, and implement operating policies and procedures regarding loan approvals and construction standards and monitoring for its single-family and small multifamily rehabilitation programs. We also recommend that HUD require the Department to (1) certify that construction deficiencies and incomplete construction work for the seven single-family properties cited in this report have been repaired or completed in accordance with the applicable standards or reimburse $394,790 to the U.S. Treasury Home Investment Trust Fund account (U.S. Treasury HOME account), (2) inspect the five multifamily properties cited in this report and certify that all applicable rehabilitation standards and housing quality standards deficiencies have been corrected or reimburse $793,775 to the U.S. Treasury HOME account, and (3) inspect 35 other properties rehabilitated under the asset control agreement cited in this report and certify that all applicable HOME program property deficiencies have been corrected or reimburse the U.S. Treasury HOME account for any properties it cannot certify. In addition, we recommend that HUD require the Department to develop and implement procedures and controls to ensure that officials enter accurate and timely HOME program data into HUD's Integrated Disbursement Information System.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of this audit.

Auditee's Response

We provided our discussion draft report to the Department on December 17, 2007, and held an exit conference on December 20, 2007. The Department generally agreed with our report findings.

The Department provided its written comments to our draft report on January 7, 2008. The complete text of the Department's response, along with our evaluation of the response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

Title II of the Cranston-Gonzales National Affordable Housing Act, as amended, authorizes the HOME Investment Partnerships Program (HOME program) to allocate grants to states and eligible local governments for the purpose of expanding the supply of decent, safe, sanitary, and affordable housing, with primary attention to rental housing, for very low-income and low-income families. The grantees carry out multiyear housing strategies through acquisition, rehabilitation, and new construction of housing. Eligible forms of assistance include loans, advances, equity investments, interest subsidies, and other forms approved by the U.S. Department of Housing and Urban Development (HUD). In addition, grantees may use HOME program funds to provide tenant-based rental assistance. In 2003, the American Dream Downpayment Initiative (Initiative) established a separate funding formula under the HOME program to provide downpayment, closing cost, and rehabilitation assistance to help low-income families achieve homeownership.

The City of Los Angeles (City) is a participating jurisdiction overseen by HUD's Office of Community Planning and Development, which executes the HOME program. Accordingly, HUD awarded $128 million in entitlement grants to the City for its HOME program in the years[1] 2004 to 2006. As required by statute, the City also budgeted $45 million in projected income (generated primarily from loan principal and interest payments) for those years from its HOME program activities to be used for additional HOME-eligible projects.

The City administers all of its HOME programs under the Los Angeles Housing Department (Department). Due to the variety of HOME program activities allowed under the law and the size of the entitlement grant, the Department divides its HOME program activities under the following major organizational units: the Major Projects Division manages the acquisition, new construction, or rehabilitation of large affordable rental housing projects; and the Homeownership and Preservation Division manages single-family or small multifamily[2] purchase acquisition projects under its Homeownership Unit and manages single-family and small multifamily rehabilitation projects under its Preservation Unit. The rehabilitation portion of the Homeownership and Preservation Division was about 10 to 26 percent of the HOME budget each year.

Table 1. City of Los Angeles HOME program resources

In millions

Program year	HOME grant	HOME income	HOME budget[a]
2004-2005	$44.8	$13.5	$61.7
2005-2006	$43.0	$15.6	$71.7
2006-2007	$40.4	$16.0	$56.9
Totals	**$128.2**	**$45.1**	**-**

[a]Includes program income and funds carried over.

[1] The amounts are awarded by Los Angeles' program year, which runs from April 1 through March 31.

[2] Single-family properties must be owner-occupied, and small multifamily projects are rental properties with 28 units or fewer.

Program year	Homeownership budget	Rehabilitation budget [a]	Rehabilitation budget as a percentage of HOME budget
2004-2005	$18.4	$12.0	19.4
2005-2006	$14.5	$18.5[b]	25.8
2006-2007	$6.0	$5.6[c]	9.8
Totals	**$38.9**	**$36.1**	**-**

[a] Rehabilitation for non-major projects.
[b] An additional $6.4 to $8.3 million was budgeted from Community Development Block Grant funds.
[c] An additional $6 million was budgeted from Community Development Block Grant funds.
Source: City of Los Angeles consolidated action plans

The objectives of our audit were to determine whether the Department (1) effectively monitored construction bids, costs, and quality; (2) ensured that borrowers and properties met eligibility requirements for income and affordability; (3) properly reported HOME program activities to HUD; and (4) properly allocated soft costs between HOME program administrative accounts and direct activity cost accounts.

RESULTS OF AUDIT

Finding 1: The Department Did Not Adequately Monitor the Rehabilitation Construction for Single-Family and Small Multifamily Properties

The Department did not ensure that all HUD-assisted rehabilitation work on single-family or small multifamily properties met applicable construction standards and/or was complete. From January 1, 2004, through January 31, 2007, the Department agreed to loan an estimated $28 million to rehabilitate 393 substandard single-family and small multifamily properties in Los Angeles. We reviewed a random sample of 27 of these rehabilitation loan activities (activities) and identified three problem areas regarding monitoring construction at the properties—a responsibility of the Department's Homeownership and Preservation Division (Division):

- Inconsistent file documentation prevented a conclusive assessment of the implementation of management controls over monitoring.
- Homeowners did not initiate rehabilitation construction work required under their single-family purchase-acquisition and rehabilitation agreements.
- The Department allowed a sole developer to monitor its own rehabilitation construction for a group of substandard properties purchased from HUD.

These problems occurred because the Department had inadequate or nonexistent policies, procedures, and controls over the construction monitoring for these HOME program-assisted activities.[3] As a result, for the 27 properties in our random sample, we observed significant construction deficiencies in four and determined that rehabilitation work was essentially not completed[4] for three. The seven properties represent a construction deficiency rate of 26 percent (see Scope and Methodology). For 12 properties we reviewed, more than $1.2 million in HOME program funds assisted, or remained obligated to assist, housing that was not decent, safe, or sanitary. We also questioned whether more than $4.8 million in HOME program funds spent for 35 additional properties rehabilitated by the developer was reasonable and/or assisted affordable housing that met rehabilitation standards.

[3] In some cases, the Department lawfully substituted HUD Community Development Block Grant funds.
[4] By not completed, we mean that at the time of our review and inspection, rehabilitation work was either not begun as required or was halted without a plan to complete the work.

Construction Monitoring Documentation Was Inconsistent

We could not assess the implementation of management's controls over rehabilitation construction monitoring because file documentation was inconsistent. Disorganized case files and multiple file locations prevented us from reviewing enough activities to conclude that management controls, such as property inspections and supervisory approvals, were adequately documented. More than half of the 17[5] randomly selected files reviewed did not provide evidence that (1) inspections were properly conducted before the work write-up, (2) reasonable costs were established by obtaining multiple bids, (3) termite or lead clearances were certified, or (4) disbursements were based on complete documentation. We noted some improvement in the more recent cases and, in some instances, officials located supplemental documentation. However, without a standard filing system for key documents, we could not test enough files to conclude that the Department adequately documented the implementation of its monitoring controls.

In addition, Department officials did not use a consistent reference for their written rehabilitation standards. In particular, the contract agencies that, for a performance fee, managed roughly half of the rehabilitation activities did not have or refer to current, written standards. Department officials later stated they had recently incorporated the standards into the online format used by staff to prepare construction work write-ups and estimates, but they did not know whether this resource was available to the contract agencies. The HOME program requires the Department to have written rehabilitation standards and to keep adequate records to document that required construction monitoring was performed and costs charged were reasonable (see appendix C for program requirements).

Construction Monitoring Policies and Procedures Were Inadequate

Construction monitoring documentation was inconsistent because the Department did not have operating policies and procedures in place regarding construction monitoring functions for its rehabilitation program. Officials interviewed generally described similar monitoring procedures, but there were no consistent or current written procedures available to all staff who monitored construction. Our file reviews revealed that, over the years, officials had implemented various forms and checklists for monitoring; however, no uniform written guidance was developed and disseminated to all staff. In addition, the officials at the four contract agencies did not refer to written guidance from the Department, although some did have training materials that were not in everyday use. Finally, although supervisory inspectors sometimes reviewed construction monitoring to resolve specific problems, the Department had no quality control program to ensure consistency. An effective quality control program could include, for example, regular

[5] We only reviewed loan approval and construction monitoring files for 17 loans in our sample of 27 because the remaining 10 were either underwritten as part of a purchase transaction or were loans made to the developer (see appendix D).

supervisory on-site inspections or random file reviews. Department officials noted that since 2005, they have centralized the rehabilitation program offices and implemented many new procedures but conceded that written guidance was under development.

Rehabilitation Construction Deficiencies Were Observed

We inspected 11 properties from the 17 files reviewed and observed significant construction deficiencies at three. Rehabilitation construction for all 11 had been monitored by the Department or its contract agencies. Senior inspectors from the Department accompanied auditors on all inspections and evaluated construction work based on the work write-ups and their knowledge of applicable standards. We observed the following deficiencies that demonstrated how the inconsistent monitoring policies, procedures, and documentation, along with inadequate quality controls, allowed substandard construction to pass monitoring reviews.

HUD Activity Number 7825

The Department paid $17,256 in HOME funds for construction work we observed to be substandard for the property identified by HUD activity number 7825. The owner, an elderly woman, was distraught that the interior paint began peeling and cracking throughout the house within a year, but the contractor did not respond to her complaints. She also stated that the contractor had used glossy paint instead of the matte texture she requested and that he talked her into accepting black tile in the bathroom, where it was previously yellow. The total HOME-funded rehabilitation loan for this property was $40,000. The following pictures show the peeling paint and other rehabilitation deficiencies that, with proper monitoring, inspectors should have required the contractor to correct. We also observed evidence of an active infestation, even though the rehabilitation work included fumigation. We concluded that either the fumigation was inadequate or the initial inspection failed to identify the extent of the infestation.

Work item	Amount paid
Electric, rewire structure	$ 2,775
Windows, aluminum replace (22)	$ 5,588
Plumbing, replumb dwelling	$ 2,928
Plaster, interior	$ 325
Plaster, interior lead related	$ 250
Drywall, repair, replace	$ 325
Paint & patch interior walls	$ 3,185
Termite fumigation	$ 1,880
Total	**$17,256**

One side of French door to sunroom was painted shut (the other side was operable).

Extensive peeling paint was observed throughout the house. The homeowner stated that this condition occurred within one year after work completion, but when she tried to contact the contractor, he had moved out of state.

A front living room window (manufactured) was defective and leaked.

The owner reported that this outlet cover was never installed in the bedroom.

There was wood debris from an active infestation in the bedroom.

A plumbing pipe was left protruding from a bedroom wall.

HUD Activity Number 8203

The Department paid a total of $490 for electrical work that included two new outlets in the kitchen of the property identified by HUD activity number 8203. The owner, an elderly woman living alone, stated that since the outlets were installed, the circuit has tripped when she does laundry and runs a kitchen appliance at the same time. Although the new outlets were installed onto the existing system, placement of the outlets on the laundry circuit violated the applicable electrical code effective as of 2002. The cost of the electrical work was small in relation to the total rehabilitation loan of $55,211. However, proper construction monitoring should not have allowed such substandard work that resulted in unnecessary hardship for the owner.

Work item	Amount paid
Electric GFI outlets	$200
Electric outlet, new	$290
Total	**$490**

New outlets were installed on an existing laundry circuit, causing the circuit breaker to trip repeatedly (code violation).

The owner also complained that the carpet in the living and dining room buckled (this was noticeable) and was a trip hazard. The Department's inspectors immediately detected that the carpeted floor lacked the proper under layer. Nevertheless, they disagreed with the auditors that the construction completion inspection should have detected this condition. According to the work write-up, the Department paid a total of $2,030 for 95 square yards of carpet in five rooms. We also observed that the new carpet buckled in a number of the properties we inspected, and the Department's inspectors stated that this condition resulted from poor installation work.

HUD Activity Number 9765

The rehabilitation construction work for the property identified by HUD activity number 9765 began shortly after May 19, 2006. However, as of our inspection in July 2007, work was well underway but still incomplete. Construction had come to a halt because the owner had many complaints about work quality and refused to sign for any more disbursements to the contractor. HUD's online Integrated Disbursement Information System (online system) showed that $28,051 in HOME funds was disbursed as of October 2006, and the project was incomplete—although $125,000 was originally approved for the loan. Proper monitoring inspections, quality controls, and written policies and procedures for owner-contractor dispute resolution could have addressed the situation before the contractor did so much disputed work.

$123,262 in HOME Program Funds Assisted Noncompliant Properties

We could not assess the implementation of management's controls over rehabilitation construction monitoring because the Department had inconsistent documentation requirements and practices over the audit period. For the 11 properties inspected, we observed that a total of $45,797 in HOME funds was used for rehabilitation work that was either substandard or incomplete. As a result, the HOME program provided $123,262 in total assistance to three properties that did not meet the rehabilitation standards. In addition, homeowner-borrowers, who generally had no funds to correct deficient workmanship, were distraught when construction work proved deficient soon after their rehabilitation work was completed.

Purchasers Did Not Contract for Needed Repairs

Four purchasers of single-family properties did not contract for required rehabilitation work within one year as agreed. The Homeownership Unit, which was part of the Division, provided Initiative funds to the borrowers under purchase agreements that included rehabilitation loans funded from the HOME program. In each case, the Homeownership Unit determined that the property "as is" did not meet the applicable HOME program standards for purchase acquisition activities. (Specifically, the inspection reports for all four of the subject properties showed that electrical work was needed.) In accordance with the HOME program regulations, both the purchase loan and the rehabilitation loan agreements stipulated that the repairs were to be completed by one year after closing. At the time of our review, purchasers of four properties, including two from our random sample, had not signed a construction contract within one year of their closing.

<u>The Department Did Not Track Construction</u>

The Department did not track the construction for these projects or take timely corrective action. For its purchase-acquisition properties, the Department contracted with an outside agency for the feasibility inspection and any later rehabilitation construction monitoring. Agency officials told us that the agency retained all of the construction monitoring documentation as the Department did not require anything to be forwarded other than the feasibility report and activity completion information. As construction deadlines approached (and construction contracts were not in place), the contract agency sent letters to the homeowners warning them that they would be in default if repairs were not completed within the required timeframes. When the homeowners did not respond, the agency also notified officials in the Homeownership Unit and officials in the construction monitoring section of the Preservation Unit. The Department had not designated an organizational unit to be responsible for tracking construction or enforcing noncompliance for these properties, and as a result, the officials did not take corrective action.

<u>Acquisition-Rehabilitation Policies and Procedures Did Not Exist</u>

Officials did not take action because once the home purchase agreement was completed, the Department had no policies and procedures to track progress and completion of the required rehabilitation construction or to enforce noncompliance. After Department officials reviewed the draft findings and investigated the issue, they concluded that improvements were also needed in the training and information provided to the lenders, realtors, and home purchasers. Officials also planned to remedy all of the property deficiencies before the audit report was issued.

<u>$421,828 in HOME Program Funds Assisted Purchases of Substandard Properties</u>

Homeowners, as a result of their failure to complete required rehabilitation work within one year, were in default for both their purchase acquisition and their rehabilitation loans. Further, HOME and Initiative funds totaling $421,828 are unsupported costs because the Department could not certify that the rehabilitation standards were met. Of this amount, $348,993 had been disbursed, and $72,835 remained committed.[6]

[6] Some of these funds were under loan contracts but were not yet committed in HUD's online system.

HUD activity number	Committed/contracted HOME funds
9949	$120,305
9805	$ 45,728[a]
9992	$129,155
10028	$126,640
Total	**$421,828**

[a] Activity 9805 also had $90,000 in Community Development Block Grant funds committed.

The Department Relied on a Developer to Monitor Its Own Rehabilitation Activities

The Department, through its Homeownership and Preservation Division or its predecessors, approved HOME program rehabilitation loans for a number of substandard properties owned by the Enterprise Home Ownership Partners (the developer) but did not monitor the related rehabilitation work performed by a sole contractor selected by the developer.[7,8] Altogether, HUD's records from 2002 forward showed that the developer received $5.6 million in HOME funds to rehabilitate 40 properties.[9]

The Department did not use its inspectors or apply its usual construction monitoring practices to these properties. Instead, it allowed the developer to monitor its own activities. Our random sample included two of these properties, and our file reviews identified deficiencies for both as follows:

- Department officials could not provide a construction monitoring file for either property, and several officials told us that the Department did not maintain construction monitoring files for any of the developer's activities because the developer was allowed to "self certify" the rehabilitation construction. The Department official who signed the disbursement request noted that often the Department disbursed the loan proceeds to the developer as one draw after construction had been completed.

- Officials provided the Department's file documentation pertaining to the loan approvals for the developer's two properties in our sample. However, we could not find the equivalent of any property inspections or cost estimates prepared or

[7] Enterprise Home Ownership Partners acquired the HUD-owned properties under an asset control area agreement among the developer, HUD, and the City. In accordance with the agreement, the Department later approved HOME-funded rehabilitation loans to the developer for each property.
[8] In 1999, Congress passed legislation that gave HUD the authority to designate local governments and nonprofit organizations as preferred purchasers of HUD-owned properties in asset control areas that met certain criteria.
[9] Loan activities for 13 of the 40 were committed in HUD's online system during the audit scope. Two of these were in our random sample. The remaining 32 were committed in 2002 or 2003.

reviewed by Department officials during a construction feasibility review such as we had found in other rehabilitation loan approval files.

- For one of these properties, the Department could not provide its own supporting documentation for the disbursement of $239,440 in HOME funds but later offered documents obtained from the developer as support.

By not monitoring the construction activities or reviewing the cost estimates, the Department did not comply with either the HOME program requirements or its rehabilitation loan agreements with the developer, which stipulated that the lender (the Department) was to preapprove the construction work write-ups and inspect the construction work.

Property Inspections Revealed Rehabilitation Work Deficiencies

Inspections of five of the developer's properties revealed that all had deficiencies in rehabilitation construction work and habitability standards. Senior inspectors from the Department accompanied auditors on inspections of the five properties, two of which were in our random sample. All five properties were three-to-five-unit rental properties and had rehabilitation completion dates from January 12, 2004, to February 12, 2005. Because up to three years had passed since construction was completed, we asked the Department's inspectors to consider and make allowances for deficiencies that could be due to passage of time and weather since completion, tenant use, or negligent management. The following are examples of conditions that we and the Department's inspectors observed at each of the five properties inspected.

Property 1: HUD Activity Number 7929[10]

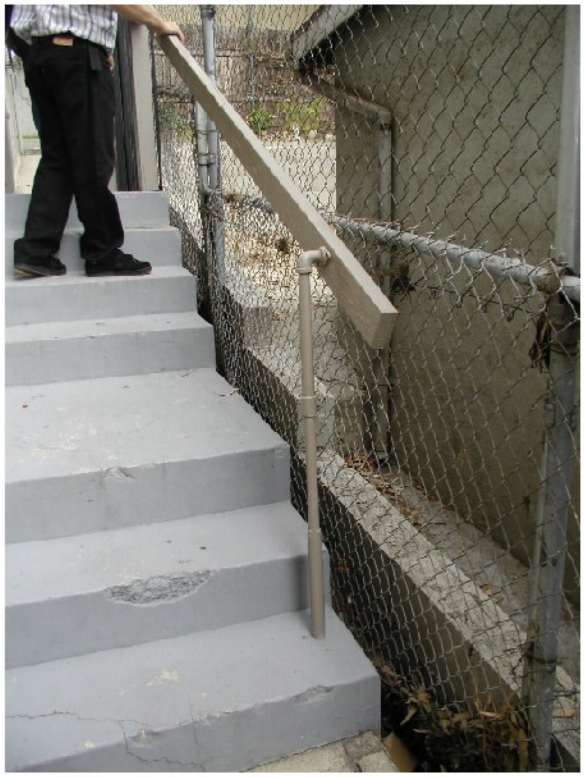
Flashing was not installed where the roof meets the house.

[10] We were not able to inspect the interior of the property for HUD activity number 7929.

There was extensive peeling paint on trim due to poor surface preparation and illegal chimney height (if in use).

Property 2: HUD Activity Number 7845

There were deteriorating steps due to poor rehabilitation workmanship and/or materials.



There was an illegal stair railing (other railings were replaced).

Rainwater downspout was not installed to deflect runoff from the front porch (hazard).

The refrigerator was in the hall because the kitchen had no space with an electrical outlet.

Property 3: HUD Activity Number 7847

Front steps were deteriorating from deficient workmanship or the repairs were never done.


Floor insulation was falling down in the crawlspace due to deficient installation work.


The second story balcony railing was too low, a hazard that was not addressed.

Extensive patching was required due to deficient paint and patch stucco work. The property manager stated that this had been a constant problem for this property. (The "before" pictures show that the house was previously yellow.)

Property 4: HUD Activity Number 8320

There were gas meters with no earthquake shut-off valves.


There was an exposed gas line in the kitchen.


There was illegal electrical grounding.

There were exposed wires in the electrical panel.

All four units had new interior water heaters installed without the required metal pan for leaks. The inspectors explained that this was a hazard, particularly on the second floor units, because leaks could cause the wood platform to rot and fail under the weight of the appliance.

Property 5: HUD Activity Number 8326

Apparently the rehabilitation converted a nonpermitted addition to meet code by raising the ceiling so that the new door would clear. However, the ceiling over the kitchen sink area was roughly six feet from the floor. The inspectors stated that although this was not technically a violation of rehabilitation or other standards, the Department would generally not have approved this design.

All windows in the three units were single pane, with the exception of two. The Department's rehabilitation standards required all windows to be upgraded to double pane.

The front steps were deteriorating, and there was a hole in the porch (covered by a board) due to deficient rehabilitation work and/or materials.

After consultation with the Department's inspectors, we judged these conditions to be the result of significant deficiencies in the rehabilitation work write-ups or construction workmanship. All deficiencies were for items that were either in the rehabilitation work write-up or were conditions the work write-up should have addressed. Our inspections also raised questions regarding cost reasonableness of the rehabilitation construction. We observed that the developer had used the same materials and presumably the same supplier for items such as carpet, flooring, kitchen cabinets, and counter tile. Accordingly, the construction costs should have reflected any volume discounts the contractor received for these items. Without reviewing cost estimates or invoices from the contractor and suppliers, the Department could not know whether appropriate discounts were applied.

The Department Did Not Follow Its Normal Practices for Approval and Monitoring

The construction deficiencies occurred because the Department did not follow its normal practices for rehabilitation construction monitoring. Instead of using its own inspectors and standards or keeping its own records, the Department allowed the developer to monitor his own contractor's work and certify the construction completion. The lack of written policies and procedures and their related controls, as described above, probably contributed to the Department's lapse. For example, the official who signed reimbursement requests did not regard his signature as certifying that required monitoring had been performed. None of the decision-making officials involved were employed at the Department during our review; however, officials we interviewed thought that, at the time, Department officials may have relied upon the building code inspections performed by the City's Department of Building and Safety. Such inspections did not meet HOME program monitoring requirements because they (1) addressed only permitted items, (2) had no information regarding the scope of work agreed upon, and (3) did not evaluate cost reasonableness. Further, officials in the construction unit did not have the information needed to initiate timely monitoring (such as project addresses, work write-ups, and construction schedules) because the Department did not commit the HOME funds until construction was completed

Housing Quality Standards Violations Were Observed

During our inspections of these multifamily properties, we also observed violations of applicable rental property standards. Although we did not attribute these violations to rehabilitation construction deficiencies, we noted that in addition to meeting standards for rehabilitation work, the HOME program required the City to monitor property conditions for HOME program-assisted multifamily rentals. The Department had inadequate property monitoring records for these properties. For example, one property with rehabilitation construction completed in 2004 was never monitored. Others were not monitored within the required three years or had no documentation that violations had been corrected.

$793,775 in HOME Funds Assisted Five Substandard Multifamily Properties

We concluded that $793,775 in HOME funds that assisted the five properties inspected was questioned costs for the following reasons:

- None of the properties met all applicable HOME program standards within two to three years after construction was completed.

- The Department did not perform or review feasibility inspections, work write-ups, and/or cost estimates for the rehabilitation work.

- The Department did not monitor the construction or review the reasonableness of costs requested for reimbursement.

- The Department did not adequately monitor the HOME program-assisted rental units to ensure that conditions were decent, safe, and sanitary.

HUD activity number	HOME funds disbursed
8320	$102,970
8326	$105,000
7845	$241,365
7929	$105,000
7847	$239,440
Total	**$793,775**

In addition, because the Department did not approve or monitor any of the developer's activities as required under the HOME program, we question additional costs of more than $4.8 million (see appendix D) disbursed to the developer for the 35 properties that we did not inspect.

Conclusion

Our property inspections and reviews for 27 randomly selected rehabilitation activities identified seven properties with construction deficiencies or construction that was not complete. We concluded that the 26 percent error rate for our statistical sample indicated that 102 of the 393 activities in our audit scope were likely to have similar problems with rehabilitation work (see Scope and Methodology). The construction deficiencies were related to the three problem areas described in this finding, which were the responsibility of the construction monitoring operations under the Division. Construction monitoring was inconsistent and sometimes ineffective in all three areas primarily because the Department lacked written standard policies, procedures, and controls that were kept up-to-date. In addition, an effective quality control program for construction monitoring would have revealed the extent of these problems to the Department. Altogether, we determined that more than $1.2 million in HOME program funds was disbursed (or committed) for unsupported costs related to 12 activities,[11] and we questioned the costs of the developer for an additional $4.8 million.

Recommendations

We recommend that the Director of the Los Angeles Office of Community Planning and Development require the Department to

1A. Develop and maintain current operating policies, procedures, and controls over construction standards and construction monitoring for all single-family and small multifamily rehabilitation activities.

[11] Seven activities were in the random sample, and five others were judgmentally selected.

1B. Certify that the construction deficiencies cited in this finding are repaired in accordance with the applicable standards or reimburse unsupported costs of $45,797 to the U.S. Treasury Home Investment Partnership Trust Fund account using nonfederal funds.

1C. Monitor and enforce the rehabilitation agreements made under its single-family purchase acquisition and rehabilitation program.

1D. Certify that the purchase-acquisition rehabilitation work cited in this finding is complete and cancel any unused portion of the $72,835 in remaining loan funds (funds to be put to better use) and, if the Department does not certify any property, require it to reimburse, using non-federal funds, the U.S. Treasury Home Investment Partnership Trust Fund account for the unsupported portion of the $348,993 disbursed for these properties.

1E. Design and implement controls to ensure that all HOME program-funded activities for rehabilitation of single family and small multifamily properties are managed in accordance with established policies and procedures designed to ensure compliance with HUD requirements.

1F. Inspect the developer’s properties cited in this finding and certify that all applicable HOME property deficiencies are corrected—using non-HOME program funds—and if this is not done, repay the unsupported portion of the $793,775 disbursed for these properties.

1G. Inspect the 35 projects listed in appendix E of this report and certify that all applicable HOME program property deficiencies are corrected or, for any properties it cannot certify, reimburse the U.S. Treasury Home Investment Trust Fund account for the unsupported portion of the $4,884,710 disbursed.

Finding 2: The Department's Loan Approval File Documentation Was Incomplete

The Department's loan file documentation for either household income eligibility or the property value was incomplete in 10 of 17 files we reviewed for compliance with loan approval requirements. In addition, our review of the processing dates, when available, showed that the loan approval process for seven files took more than six months. Documentation was inadequate because the Department did not have a standard set of written policies and operating procedures. Loan processing times were excessive because, overall, the Department did not establish or monitor target timeframes. As a result, the HOME program may have assisted ineligible households and/or rehabilitated properties with values that exceeded the HOME limit. Also, processing delays made it difficult for the City to meet its HOME grant commitment deadlines and consolidated planning goals.

Documentation of Zero Income Was Inadequate

Adult household members did not certify that they had no income for 7 of 17 loan approval files reviewed. For example, some households included an unemployed adult but did not have evidence of social security payments or student exemption. In one case, the Department requested that the borrower certify that three other adults in the household had no income (the adults themselves did not make—or were not asked to make—the certification). However the borrower's certification letter was more than six months old by the time the loan was approved. Further, in this case and one other case, the household qualified only because it included one or more adults without income.[12]

HOME program regulations require record keeping to demonstrate that each family is eligible. The Department's income documentation did not ensure that claims of no income were valid in households like those described above. Accordingly, the Department's risk of waste, fraud and abuse of its HOME program funds was increased because it did not adequately support claims of zero income for all adult household members

Property Values Were Not Fully Supported

The after-rehabilitation value of the property was not fully supported in 8 of the 17 loan approval files we reviewed. The HOME program regulations are flexible regarding the

[12] The income limit increases with the number of household members.

methods available to establish property value, and the Department used various approaches over the audit period. However, the records did not always demonstrate how the estimated value was determined, as required by the regulations. For example, we could not determine which comparable properties were used or not used and why. In other cases the comparable property values were more than six months old by the time the loan was approved. Accordingly, the Department could not certify that the values of these rehabilitated properties were within HOME program limits.

In some cases, the Department substituted funds from the Community Development Block Grant program, which has no property value limit. This policy is acceptable; however, the Department should document its policies for funding sources and note the income eligibility requirements that still apply to Community Development Block Grant-funded loans.

Loan Processing Times Were Often Excessive

The Department typically took more than six months to process a loan from its application date until the notice to proceed was issued. For 12 loan files reviewed,[13] the average processing time was 10 months, and for seven of the loans, it exceeded six months. Officials reported that long processing times had caused borrowers to drop out of the program. As a result, the Division did not commit a significant portion of budgeted HOME program funds or meet its consolidated planning goals in 2004. In turn, this situation made it more difficult for the Department to meet regulatory deadlines for overall HOME program commitments.

Standard Policies and Procedures Were Not Maintained

The officials who processed loan applications did not follow consistent policies and procedures because the Department did not have a standard set of written policies and procedures that were up-to-date and readily available to all finance officers/underwriters—both in-house and at contract agencies. Officials we interviewed from the Department as well as the agencies seemed to understand the HOME program requirements. They listed many documents that were available to verify requirements such as income eligibility, home ownership, and household size. However, the files we reviewed typically had minimal documentation. For example, we rarely found bank statements or third-party verifications. Neither the Department nor the contract agency officials provided written operating policies and procedures for eligibility determinations that were used by all of the underwriters. Although some of the agencies provided application packets that included a "statement of no income" document, there were no

[13] We only analyzed this timeframe in 12 of the 17 loan files because five did not include the dated application and the Department did not track these dates.

written instructions or procedures that required adult household members without income to sign a statement (unless they were the borrower.) Likewise, the Department's guidance for determination of property values was not consistently documented.

Conclusion

The Department's shortcomings in loan approval documentation and processing time stemmed from its lack of uniform operating policies and procedures that are kept up-to-date and made available to all loan processors, both in-house and agency. The Department could not demonstrate its compliance with HOME program eligibility requirements because file documentation was incomplete. Moreover, inconsistent file documentation standards can lead to waste, fraud, or abuse if HOME funds assist ineligible households or properties. Finally, performance standards that include target timeframes for loan processing would improve customer service and help the Department use its HUD grants more efficiently.

Recommendations

We recommend that the Director of the Los Angeles Office of Community Planning Department require the Department to

2A. Develop and annually update operating policies and procedures for loan approval that apply to all activities that are approved under the Homeownership and Preservation Division.

2B. Develop and implement quality control procedures that periodically document supervisory quality control reviews for a representative sample of files and provide for corrective action when necessary.

2C. Develop and implement loan processing performance standards to improve timeliness.

Finding 3: The Department's Status of Activities Was Not Reported to HUD in a Timely Manner

The Department did not enter activity commitment or completion data into HUD's online system in a timely manner for a significant number of rehabilitation projects. This condition occurred because the Department's project management database(s) were not integrated with HUD's online system. Further, the Department had no controls or procedures in place to ensure timely and accurate manual data input. HUD depends on accurate reporting to its online system for effective grant monitoring. Inaccurate data can delay needed corrective actions and lead to sanctions by HUD if commitment and disbursement deadlines are not met.

Committed Funds and Completed Activities Were Reported Late

The Department did not enter activity commitment data into HUD's online system in a timely manner for a significant number of rehabilitation activities. We analyzed the 17 activities in our random sample that were rehabilitation-only (and not managed by the developer as discussed in finding 1) and found that six activities had funds committed in HUD's online system more than six months after the loan approval.[14] HUD guidelines require data in its online system to be updated quarterly.

Also, the Department did not enter the project completion status into HUD's online system within the required 120 days for a significant number of rehabilitation activities. For the 17 rehabilitation-only activities we selected, 12 had been completed. Eight of these had sufficient data for analysis, and HUD's online system showed that for six of the eight, more than 120 days had elapsed from the final disbursement date until the Department entered a status of "complete." The average time was nine months.

Procedures and Controls over Manual Data Entry Did Not Exist

The Department had no controls or operating procedures in place to ensure timely and accurate reporting to HUD's online system. Officials had to manually enter HOME program data into HUD's online system because the Department's project management database(s) were not integrated with HUD's. During our review, Department officials could not provide written guidance regarding who was responsible for entering HOME

[14] For the developer activities discussed above, funds were routinely committed after the construction was completed.

program activity data into HUD's online system, when data should be entered, or what documentation was required (and should be maintained) to support that data entered were valid. Within the Division, access to HUD's online system was apparently restricted to a small number of staff, as appropriate. Although the Department had conducted a data cleanup effort in 2004, no procedures to maintain data integrity or perform periodic reconciliations were developed because the Department expected to implement a new information system that would be integrated with HUD's. The new system did not work properly, and at the time of our report, the Department was developing another system. Officials noted that anticipation of the new system had distracted them from developing needed procedures and controls over manual data entry.

HUD Relies on Timely Reporting

HUD relies on the data in its online system to remotely monitor the funding and performance of the HOME program—and other entitlement grant activities. Inaccurate data reduce the effectiveness of HUD's remote monitoring for compliance with commitment deadlines and other program requirements. In addition, poor data reliability in HUD's online system raises questions regarding the City's overall management of its HUD entitlement grant programs. As a result, HUD and other reviewers must perform additional on-site work to effectively evaluate the City's compliance with program requirements.

Conclusion

The Department did not enter HOME program activity data into HUD's online system in a timely manner because it had no policies, procedures, or guidance regarding reporting HOME program activity data to HUD. Further, the Department did not periodically reconcile its own project database information with HUD's to ensure that manual reporting was accurate. As a result, the Department could not effectively monitor its own compliance with statutory deadlines for commitments and disbursements or other program requirements. Based on the inaccurate data, HUD could impose sanctions or fail to initiate needed corrective action.

Recommendations

We recommend that the Director of the Los Angeles Office of Community Planning and Development require the Department to

3A. Design and implement procedures and performance benchmarks that ensure all of its departmental units enter accurate and timely HOME program data into HUD's Integrated Disbursement Information System.

3B. Periodically reconcile the activities in its project database(s) to information in HUD's Integrated Disbursement Information System.

Finding 4: The Department Improperly Allocated Administrative Costs to Projects

The Department improperly allocated some administrative costs to HOME program direct activity costs in HUD's online system. In one instance, the Department allocated ineligible administrative costs because it did not use a job costing system to directly capture the staff time spent on specific activities. In another instance, the Department did not change the contract agency fee from a direct cost to an administrative cost when the project was cancelled. This condition occurred because the Department had no formal procedures to process cancelled activities. As a result of both errors, the HOME program administrative costs, which the regulations cap, were understated in HUD's online system.

Soft Cost Allocation Formula Included Ineligible Expenses

For one program year, the Department allocated some ineligible administrative expenses to direct costs for rehabilitation activities. The HOME program allows certain program delivery costs (soft costs) such as staff underwriter salaries to be charged either to the HOME program administrative fund or to the related activity's direct costs[15] as long as the rehabilitation work was completed. Because the HOME program caps the annual administrative costs at 10 percent and also limits the total amount that can be charged directly to each rehabilitation activity, the option to apply the soft costs to either provides some flexibility.

Historically, the Department had charged all of its rehabilitation staff salaries to the administrative fund, despite the opportunity to charge a substantial portion directly to activities. However, officials said that for program year 2006,[16] the Department's administrative charges exceeded the cap. To comply with program rules, officials allocated staff costs to rehabilitation activities based upon each activity's proportion of the HOME disbursements that year. The staff costs included salaries for underwriting and construction monitoring staff in the Division, as well as the associated benefits. However, officials also applied the City's cost allocation plan formula to the salaries, effectively adding a portion of overhead costs, such as utilities, which were ineligible according to HOME regulations. We did not determine whether the overall allocation method was in compliance with federal requirements.

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[15] The administrative fund and the direct activity costs both refer to the fund classifications in HUD's online system.

[16] Program year refers to HUD's online system report for 2006, which covered the period April 1, 2005, through March 31, 2006.

Activity Accounts Did Not Directly Capture Staff Time

The Department did not have a job costing system to directly capture the staff time spent on specific HOME program or other activities. As a result, the Department could only apply staff costs for program delivery to direct activities by using an allocation formula. Officials stated that they did not plan to use the allocation formula in the future. Further, the Department was testing a new electronic timesheet system that would eventually capture staff time by activity. After this finding was presented to the Department, officials stated that they moved the ineligible costs to the administrative fund; however, we did not verify this change. Since the amount was relatively small and officials did not plan to repeat the practice, we did not formally recommend the adjustment.

Procedures to Cancel Activities Did Not Exist

The Department had no procedures in place to ensure that soft costs charged to a direct rehabilitation activity in HUD's online system were transferred to the administrative fund if the activity was cancelled (or not completed). Our sample review included one cancelled loan; however, the contract agency performance fee for this activity was still reported to HUD as a direct cost. Although accounting officials stated that the rehabilitation staff should have alerted them to reassign the fee, the Department had no procedures in place regarding data entry into HUD's online system, as discussed in finding 3.

Administrative Costs Were Understated in HUD's Online System

To the extent to which it charged ineligible soft costs to direct activities, the Department understated its HOME administrative costs in HUD's online system. Further, the Department was at risk of exceeding the 10 percent cap for annual HOME program administrative expenses because it also used the soft cost allocation plan to distribute salary costs to activities under its Major Projects Division. Finally, rehabilitation projects managed by contract agencies were charged more than their fair share of the soft costs because the Department had already charged the performance fees to the direct activities.

Conclusion

The Department charged some ineligible administrative costs to direct activity costs in HUD's online system. Although most of the ineligible charges resulted from a one-time allocation of rehabilitation staff costs to activities in 2006, HUD should review any future plans to allocate soft costs to activities. Also, the Department needs to establish controls over its data in HUD's online system, as discussed in finding 3, to ensure that administrative costs incurred for cancelled activities are properly charged to the administrative fund.

Recommendations

We recommend that the Director of the Los Angeles Office of Community Planning and Development

4A. Review any future allocation of staff costs to direct rehabilitation project costs and require the Department to document its rationale for any allocation formulas.

4B. Require the Department to establish controls to ensure that staff costs or performance fees already charged to a project are transferred to the HOME administrative fund if the project is cancelled.

SCOPE AND METHODOLOGY

Our audit focused on the City's rehabilitation loan activities funded primarily by the HOME program to increase affordable housing for owner-occupied single-family and small multifamily properties. The City also used a major portion of its HOME program funds to construct, acquire, and/or rehabilitate large multifamily affordable housing properties; however, we excluded these from our audit scope.

We gained an understanding of how the City administered its HOME grants through interviews with officials from the

- HUD Office of Community Planning and Development in Los Angeles;
- Los Angeles Housing Department and its Homeownership and Preservation Division, which manages the purchase and/or rehabilitation of single-family and small multifamily properties;
- Los Angeles Community Development Department, which prepares the City's annual action plans and consolidated annual performance evaluation reports for the entitlement grants;
- Los Angeles Office of the Controller, which performs internal audits of City departments;
- Los Angeles Neighborhood Housing Services, a contract agency;
- Slauson-Avalon Citywide, a contract agency;
- Kedren Park Citywide, a contract agency; and
- Vermont Slauson Economic Development Corporation, a contract agency.

To accomplish our audit objectives, we reviewed

- The applicable federal laws, regulations, and HUD guidance for the HOME program and for affordable housing rehabilitation activities funded by the Community Development Block Grant program;
- The Office of Management and Budget regulations for local grantees;
- HUD monitoring reviews;
- Reports from HUD's Integrated Disbursement Information System;
- The City's annual action plans and consolidated annual performance evaluation reports;
- The Department's policies, procedures, and file documentation;
- Applicable sections in national, state, and local building codes; and
- Internal audit reports from the City's Office of the Controller.

Information in HUD's online system identified 393 single-family and small multifamily properties with funds committed for rehabilitation loans from January 1, 2004, through January 31, 2007.[17] We included properties that received purchase assistance as well as rehabilitation

[17] We analyzed the Department's commitments in HUD's online system to identify properties with rehabilitation loans within our audit scope. We initially identified 451 properties for which the Department committed more than $32 million. However, testing determined that some records represented properties that should have been excluded (such as loans recorded as purchase and rehabilitation that turned out to be purchase-only), and, therefore, we estimated the actual universe to be 393 properties.

assistance, but we did not review the purchase loan approval process. Using the commitment information in HUD's online system, we randomly selected 27 activities to review. Appendix D presents information on the 27 sample activities.

Our audit determined that rehabilitation construction for 7 of the 27 sample activities was either substandard, not complete, or never begun. Accordingly, our statistical analysis estimated that similar construction deficiencies were present for 102 rehabilitated properties in the universe of 393, for a construction deficiency rate of 26 percent. We did not project the amount of ineligible costs we found for the seven sample activities to the universe because our sample plan was designed to test controls.

Senior construction specialists from the Division accompanied auditors to all on-site inspections to evaluate whether rehabilitation work was performed in accordance with the work write-ups and all applicable rehabilitation standards. To the extent possible, the specialists also considered the cost reasonableness of the work items. We consulted with the specialists to distinguish between deficiencies that were the result of substandard rehabilitation work and deficiencies that were violations of housing quality standards and, therefore, could have been caused by the occupant or negligent property management. In addition to the 13 sample properties, we inspected three properties rehabilitated by the developer that had been judgmentally selected from our audit universe. During the inspections we interviewed property owners and managers.

We conducted our fieldwork from February though October 2007 at the City's office in Los Angeles, California, and performed the audit in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Policies and procedures to ensure that HOME program grants are carried out in accordance with applicable laws and regulations.

- Policies and procedures to ensure that HOME program grant expenditures are eligible and adequately supported.

- Policies and procedures to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

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

- The Department did not have adequate policies and procedures to ensure that rehabilitation construction for single-family and small multifamily properties was carried out in accordance with applicable laws and regulations (finding 1).

- The Department did not have adequate policies and procedures to adequately support that its HOME program participants were income eligible and/or that property values were within program limits (finding 2).

- The Department did not have policies and procedures to reasonably ensure that valid and reliable data were reported in a timely manner to HUD’s online system (findings 3 and 4).

APPENDIXES

Appendix A

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

Recommendation number	Unsupported 1/	Funds to be put to better use 2/
1B	$45,797	
1D	$348,993	$72,835
1F	$793,775	
1G	$4,884,710	
Total	$6,073,275	$72,835

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 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. In this situation, costs were charged for rehabilitation construction work that was observed to be substandard or incomplete. As a result, HOME funds were used for housing that did not meet all applicable property standards, as required by the HOME program. Also, the amount of unsupported costs in recommendation 1G is for HOME funds that the Department disbursed to the developer without adequate monitoring and record keeping for the rehabilitation construction on 35 properties.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. This includes reductions in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings which are specifically identified. In this instance, the HOME funds were committed, or contracted to be committed, for rehabilitation construction that had not been performed as required at the time of our report.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

OFFICE OF THE GENERAL MANAGER
Los Angeles Housing Department
LAHD
1200 W. 7th Street, 9th Fl, Los Angeles, CA 90017
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www.lacity.org/lahd

Antonio R. Villaraigosa, Mayor
Mercedes Márquez, General Manager

January 7, 2008

Joan S. Hobbs, Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General, Region IX
611 West 6th Street, Suite 1160
Los Angeles, CA 90017-3101

Dear Ms. Hobbs:

Enclosed is our response to the findings and recommendations of the recently completed audit of the City of Los Angeles Housing Department's (LAHD) HOME Investment Partnership programs. Management and staff of LAHD appreciate the time taken by the Office of Inspector General (OIG) audit staff to conduct a thorough assessment and your willingness to discuss issues and to hear our point of view.

As noted in the response, the Department had identified many of these problem issues and had begun to make improvements in the organizational structure and staffing during program year 2005-2006. Many additional changes, including the development of a written Operations Manual, while in process, had not been finalized by the time the OIG audit was competed.

LAHD looks forward to working with HUD to further improve the program's efficiency and effectiveness. If you have any questions, please contact me or Doug Swoger, Housing Director of Homeownership and Preservation, at 213-808-8948.

Sincerely,

MERCEDES MÁRQUEZ
General Manager

Enclosure

cc: William Vasquez, Director
Region IX, Office of Community Planning and Development

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Background

Concerns about the Housing Department

Prior to the appointment of the current General Manager (GM) in January 2004, the Mayor, the City Council, and public stakeholders had expressed concerns about the state of affairs at the Housing Department, particularly, in regard to its management and productivity. When appointed as General Manager, Mercedes Márquez promised to conduct a comprehensive assessment of the Department in response to these concerns. The GM completed her assessment in late 2004 and presented it to Council in a report called "Reinventing the Housing Department: Reorganizing to Preserve and Produce More Housing." Council approved the recommendations which were then implemented in 2005. However, the GM and her Assistant General Managers (AGM) continue to identify and rectify problems and issues at the Division, Unit and Program levels in order to improve in efficiency, effectiveness and productivity.

The Los Angeles Housing Department (LAHD) has almost 600 employees in three Bureaus with twelve Divisions containing more than thirty Business Units, each operating several different programs. All programs were preliminarily assessed and changes were initiated in critical areas. The General Manager and her staff worked on several tracks simultaneously: reviewing the performance of staff, particularly, management staff of the Business Units; updating hiring tests, positions and outdated job descriptions in order to recruit more qualified and highly skilled employees; and providing staff with training to ensure an understanding of program requirements. By the time the OIG had initiated their audit of LAHD's housing rehabilitation programs, all of the senior and mid-management staff had been replaced and new staff either hired or being recruited. The extent of the problems were such that they could not all be rectified by the time the audit was initiated.

The City's housing rehabilitation programs are located in the Homeownership and Preservation Division within the Housing Development Bureau of the Housing Department. The primary purpose of this Bureau is to create and preserve affordable housing and expand homeownership opportunities. Multifamily new construction and rehabilitation loans are made to qualified developers through a competitive Notice of Funding Availability (NOFA) process. First-time homebuyers or property owners who wish to rehabilitate their properties may apply directly for loans through the Purchase Assistance, Purchase Assistance with Rehabilitation, and Comprehensive Housing Rehabilitation programs. Loan amounts can range from $50,000 to $14 million, with smaller loans provided for single-family rehabilitation and home ownership, and larger loans provided for multifamily new construction or major rehabilitation. With the exception of the Moderate Income First Time Homebuyers Programs, all housing financed through these programs benefit lower-income residents of Los Angeles.

Improvements in Productivity

When the Housing Development's portfolio and programs expanded rapidly between 2000 and 2004, the organizational systems, staffing, training, and policies and procedures did not keep pace, leading to serious problems that needed to be rectified. There was a general lack of management oversight prior to 2005, which the General Manager discovered in her assessment and began to correct in reorganizing the Housing Department. There were numerous obvious concerns to be addressed and, initially, it was unclear how pervasive that lack of oversight was. Upper management staff focused on dealing with management problems and improving the hiring infrastructure to get the highly skilled staff in place needed to fix the programs.

There were many pressing demands and competing priorities, in the Housing Development Bureau, the AGM and her staff started working in those areas with the highest dollar volume and impacts: Portfolio Management, loan originations from the Major Projects Division (including the Affordable Housing Trust Fund (AHTF)); and loan originations for first time homebuyers from the Homeownership and Preservation Division.

These efforts have resulted in significant improvements in productivity increasing production of rental and ownership units many-fold. As results of those changes, there is a standardized RFP, procedures and funding cycle for the Affordable Housing Trust Fund (AHTF) and a greatly improved Major Projects reports and records unit. Improvements in productivity of the AHTF are shown below.

Calendar Year	# Projects	# Units	Amount of LAHD Funds	Amount of funds leveraged
2003	16	933	$ 38,687,352	$ 135,913,404
2007	26	1,521	$ 108,345,697	$ 344,362,565

The low income first time homebuyer program was overhauled and, as a result, loans have grown from $3.5 million (61 low income loans) in 2004 to $16.25 million (137 low income loans) in 2007.

Portfolio Management has been given the management support it needed to analyze delinquencies and proceed with foreclosures, as appropriate. (It should be noted that Los Angeles is one of few cities in the country that actually forecloses on properties when the owner is in violation of the loan agreement and obtains repayment of loans made with HOME and CDBG.) As a result, the current "over 90 days plus" delinquency rate for the LAHD portfolio of 4652 loans is approximately 3.1%. These are single family and multifamily loans, almost all of which are in second or third position and are considered to be much more risky than first mortgage loans. This rate compares favorably with Mortgage Bankers Association data that the "over 90 days plus" delinquency rate in the third quarter of 2007 is 1.31% for conventional first mortgage loans and 5% for government insured mortgages.

Changes were also made in the housing rehabilitation programs between 2005 and 2007, addressing glaring problems within the program. These improvements will be discussed in context of each finding. Due to the relatively small dollar volume of the housing rehabilitation programs – 9.6% in 2006[1] -- and changes in staffing that occurred in 2006, this has been the last group of programs to be comprehensively analyzed and upgraded.

Reorganization of the Housing Rehabilitation Function
Prior to 2005, the housing rehabilitation program (called the Neighborhood Preservation Program (NPP)) was located in satellite offices throughout the City. Regardless of the number of loans processed, each office had an office supervisor, a loan specialist, a rehab construction specialist and a clerk-typist. Although the offices were supposed to

[1] Although the housing rehabilitation budgets were significantly higher in 2004-2005 and 2005-2006, the actual amount expended was approximately $5.5 million in each of those years. This is why the budget was reduced in 2006-2007.

be managed by a main office staff group with expertise in loans and construction, each office functioned independently of each other and of the main office. There were no written standardized policies and procedures for the satellite offices, although a few created their own. Production was very low for such extensive staffing and the quality of loan and rehab construction files -- and work -- varied widely among offices. Recognizing that this outdated infrastructure designed almost 20 years earlier was unproductive, the GM instituted the reorganization of the housing rehabilitation function.

There were also Contract Agencies (CAs) that carry out housing rehabilitation activities on behalf of the City. These agencies were established to provide additional rehab assistance to city residents after the 1994 Northridge earthquake. Prior to 2005, the CAs were monitored by Management Analysts who did not have a background in housing rehabilitation.

In December 2004, the Department finalized the reorganization that created the Homeownership and Preservation Division[2]. The rehabilitation construction function was separated from the loan function and three units were created to operate the housing rehabilitation programs. They were:

- the Comprehensive Rehabilitation programs section which originated housing rehabilitation loans;
- the Contract Agency Monitoring Unit which reviewed and approved Contract Agency loan packages; and
- the construction Technical Services Unit (TSU) which inspected properties, developed the work write-ups, and conducted construction oversight and monitoring for the Division's rehabilitation projects. In addition, this unit was responsible for two other functions:
    - monitoring the Contract Agencies construction activities, and
    - monitoring the rehabilitation portion of Homeownership's purchase assistance with rehab program.

When the reorganization was completed in early 2005, housing rehabilitation staff were brought in from the satellite offices, centralized downtown and reassigned to one of the three units. For the first time, Contract Agencies' work was monitored by LAHD staff members who were specialists in loan packaging and construction. This was a difficult adjustment for all. A number of Contract Agencies complained about the oversight. Many staff members were resentful that they were no longer out in the field on their own and resisted being integrated into the new system.

HUD Monitoring and Technical Assistance

Comment 1

The most recent written HUD monitoring report reviewing CDBG and HOME funded activities was for the program year 2004. Conducted in the summer and fall of 2005 and received in February 2006, it discussed a number of issues but did not show problems that were surfaced by the OIG audit. Although HUD staff conducted monitoring activities

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[2] This Division included the Comprehensive Rehabilitation Programs, the Contract Agency Monitoring Unit, the Technical Services Unit, the Homeownership Unit, the Handyworker Program and the Lead Programs.

in 2006 and 2007, only preliminary findings have been revealed and did not appear to include the issues discussed herein.

While HUD approved LAHD's technical assistance request in 2004, LAHD's January 2006 request to HUD for in-depth technical assistance to develop clear, detailed, policies and procedures for HOME program operations was turned down. That request described the same problems identified by the OIG Representative in the following year, i.e., "[p]olicies and procedures manuals for these programs are out of date and ineffective. The lack of specified procedures sometimes leads to inefficient and untimely loan processing." Although LAHD staff and consultants continued to work on fixing these problems while operating programs; written program operations manuals were not in place at the time of the audit.

Finding 1: The Department did not adequately monitor the rehabilitation construction for single-family and multifamily properties.

1.1a Construction monitoring documentation was inconsistent[3].

LAHD Response

We agree that this was true of files created ***prior*** to 2006. Of the files randomly selected by the OIG for audit, approximately 70% were created prior to 2006 (even though their IDIS Commitment date might have been 2006). In 2005-2006, significant changes were implemented by the TSU Supervisor. It took about six to eight months before the forms, formats, work write-ups and specifications were implemented on a consistent basis. We believe that a review of construction and disbursement files created in 2006 and 2007 would demonstrate appropriate management controls, including property inspections, construction monitoring, and supervisory approvals.

One problem in reviewing these files was LAHD's policy of maintaining two files related to construction, a construction file and a disbursement file. Originally, when the OIG Representative requested the construction files for each project, she was given only the construction, and not the disbursement files. When it was ascertained that she had not received complete construction documentation, the disbursement files were provided. As a result of this audit, we have seen how difficult it is to track and document projects consistently using the two file system. Therefore, procedures have been established to utilize a single comprehensive construction file beginning in 2008.

Finding 1.1b: Department officials did not use a consistent reference for its written rehab standards.

Comment 2

LAHD Response:

We disagree with this finding. Particularly in the TSU, rehab construction specialist's skills and knowledge varied widely even though staff members had been in their jobs for many years. In order to create a uniform, thorough process, the TSU Supervisor revised the property inspection form and inspection procedures and made them more comprehensive and specific to reduce the possibility that needed repair items would be overlooked during the property inspection. He also updated the property specifications and integrated them into a work write-up/specifications writing system in MS-Word. This was done so that contractors -- and rehab specialists – only had to look in one place for the complete repair requirement; as opposed to needing to look at the work write-up *and* at a separate book of rehab standards.

In 2005, after the TSU Supervisor updated the property inspection form, rehabilitation specifications, work write-up and construction monitoring forms, and timelines, there was a meeting with staff to review the new forms, process and procedures. The forms, formats, and checklists were placed on the computer drive utilized by TSU staff so they could easily utilize them. There was also a separate meeting with CA staff to do the same. CAs were provided with disks that contained the new system and all forms. A letter was sent to the CAs instructing them to utilize the new system from April 2005 onwards.

Despite the fact that it took almost a year to achieve consistency, the Department and its CAs used a standard written set of rehabilitation standards that were integrated with a

[3] The Audit Report does not break this category into Findings 1.1a and 1.1b; however, separating them in this way makes the response clearer.

computerized work write-up system (in MS-Word) so that contractors did not have to look at two different sources of information to bid projects. It is quite possible that the LAHD and CA staff who use this system do not think of it as a written manual of specifications and, conveyed that impression to the OIG Representative.

The TSU supervisor printed out a copy of the specifications for the OIG Representative and explained that the information is updated on an as needed basis when there are changes in the marketplace. This not a very sophisticated system because it is used by many people with varying computer skills at the main office and in Contract Agencies, but we believe that it meets the HOME requirements for written rehabilitation standards. Based on the OIG Representative's suggestion, as of January 2008, those specifications will be placed on the LAHD website, available to all interested parties, and staff will update them on a quarterly basis.

Finding 1.2 Construction Monitoring policies and Procedures Were Inadequate
LAHD Response
We agree. Although a lot of time and effort went into providing LAHD staff and CAs with updated forms for every aspect of the construction process, checklists and Tables of Contents (for construction files), there was no single written document to which they could turn to find the policies, procedures, checklists and forms together in a comprehensive whole.

The current Director of Homeownership and Preservation was hired for his expertise in housing rehabilitation programs and charged with fixing problems in the rehab programs. Unfortunately, the OIG began its audit prior to the Director being hired and completed it while changes were underway. Since the Director was hired in January 2007, he has evaluated the programs and assessed the staff. He has made critical changes and developed written guidance in a number of areas including the rehabilitation construction process, quality control (both at LAHD and in the CAs), supervisory procedures and performance standards. Development of these policies and procedures were underway, but not completed, when the OIG completed its audit. Staff and CAs will receive training in these policies and procedures in January 2008 and they will be placed on the LAHD website.

Finding 1.3 Rehabilitation Construction Deficiencies Were Observed
LAHD Response

Comment 3

Where construction deficiencies exist as a result of inadequate construction monitoring, LAHD will repair them. Additionally, LAHD is reviewing all correspondence related to the rehab programs to identify other projects where complaints have been made. The Director or Rehabilitation Program Manager[4] will review the complaint, go to the complainant's home to view the problems, and LAHD will repair those properties if it appears that inadequate construction monitoring allowed poor quality work.

Comment 4

Although the paragraph heading in the Audit Report said that "$123,262 in HOME Program Funds Assisted Noncompliant Properties," the costs to be repaired appear to be a total of approximately $46,000. Two of the three cases, noted in the Audit were initiated prior to 2005 during the time when the rehab construction specialists (RCSs)

[4] Both assumed their positions during 2007; the Director in January and the Rehabilitation Program Manager in November.

were located in District offices virtually unsupervised. It was this lack of management and technical oversight that caused the GM to eliminate the inefficient infrastructure and centralize the housing rehabilitation program staff in one location at the main office.

Comment 5

Finding 1.4 Purchasers Did Not Contract for Needed Repairs
LAHD Response
This finding has been resolved. The $421,828 cited in the Audit Report for purchasers who did not contract for needed repairs are no longer unsupported costs. In fact, this problem has been completely resolved and those homeowners and LAHD are in compliance.

When this problem was brought to management's attention, several activities took place:

1. The scope of the problem was identified – how many projects, over what period of time;
2. Letters were written to each of the borrowers explaining the program, telling them that they were currently in default of their obligations and, if the required repairs (or contract for rehab) were not made within sixty days, LAHD would foreclose;
3. A senior RCS was assigned to work with these borrowers and the Contract Agency working with them, and to review the inspection list, check for permits and go onsite to view the repairs; and
4. Lenders and realtors participating in the program were expressly informed of the program requirements during their semi-annual meeting with staff.

Written procedures were put in place to ensure that this does not happen again.

1. A brochure was developed and will be sent to loan applicants, lenders, and realtors that clearly states the program requirements;
2. A staff member was assigned to call each "priority" reservation[5] to discuss the program requirements. After the conversation, a follow-up note is mailed to the prospective borrower;
3. The loan officer now highlights those sections of the loan documents that refer to the requirement to bring the home up to code the borrower initials that s/he has read and understands that section;
4. A LAHD RCS has been designated as the CA construction monitor and is the responsible party for tracking compliance and working with the Rehab Program Manager will determine how compliance will be enforced for the properties. These procedures are contained in the new operations manual; and
5. The Contract Agencies now provide monthly information to the LAHD regarding all cases requiring rehab. If two months have gone by since purchase loan closing without any construction related work, the LAHD construction monitor will work with the agency and the borrower to get the rehab underway.

As a result of these actions, ***all*** first time homebuyers whose homes required repair have either completed their repairs according to code and the repairs have been inspected and approved or they have signed their rehab loan agreements and are in the rehab construction process.

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[5] Those applicants who have a real estate contract to purchase a home.

Finding 1.5 The Department Relied on a Developer to Monitor Its Own Rehabilitation Activities
Finding 1.5.1 Property Inspections Revealed Rehabilitation Work Was Deficient
LAHD Response
These projects were part of a 2000 Agreement that LAHD entered into with the nonprofit organization, Enterprise Homeownership Partners (EHOP) and the US Department of Housing and Urban Development (HUD). Pursuant to the Agreement, EHOP was to acquire 1-4 unit HUD-owned, foreclosed and unsold properties, rehabilitate and resell the properties to qualified buyers. In 2005, HUD Central sent auditors out to review the EHOP files and projects under construction. These auditors made no findings regarding the property rehabilitation.

Comment 6

The properties to which this finding refers were rehabilitated during the period 2002 thru 2005; the majority, 19 projects, were rehabilitated in 2002 and 2003, eleven were completed in 2004 and five projects completed in 2005. We acknowledge the key point of this finding, that LAHD did not oversee these projects appropriately. The General Manager has assigned the Systematic Code Enforcement Program (SCEP), HOME Monitoring Unit, to inspect each of the 35 properties for construction defects and HOME monitoring compliance. This unit will begin to inspect these properties in January 2008 and will be completed by the end of February. The inspectors in this unit are not connected with the Homeownership and Preservation Division in any way. They are experts in code compliance and have been trained in HOME monitoring. They will provide an impartial assessment of what needs to be done by LAHD, EHOP, and the current property owners to meet HOME standards. Repairs will begin as soon as a SCEP inspection report is received for a property.

Comment 7

Finding 1.5.2 The Department Did Not Follow Its Normal Practices for Approval and Monitoring
LAHD Response
At some point, between 2002 and 2005, the former, and now retired, Director of Homeownership and Preservation decided to change the construction management procedures outlined in the EHOP loan agreement. He decided that there would be a single inspection by LAHD staff at project completion. This final (and only) inspection and signed-off permits would verify that all construction work had been properly completed in accordance with the project scope of work. Although staff speculated to the OIG Representative about why this occurred, he is no longer with LAHD and we don't know the exact rationale for his decision. He might have thought that the interim inspections by code inspectors would be sufficient prior to a final inspection by the rehab staff, since work would not be paid until after a final inspection.

Comment 8

Finding 1.5.3 Housing Quality Standards Violations Were Observed
LAHD Response
There appears to have been no system in place for transferring these projects from Occupancy Monitoring to the SCEP HOME Monitoring Unit for property inspections. Although the Finance Officer working on the EHOP projects sent a list of properties to Occupancy Monitoring, that list was not forwarded to the HOME Monitoring Unit.

A number of changes in how LAHD conducts HOME monitoring are underway. New procedures with feedback loops will be completed by the end of February so that we all can be assured that these units are in the occupancy monitoring and property inspection system. As needed, staff in these units will be re-trained in HOME requirements to ensure that they understand the importance of this on-going function.

As described previously, SCEP's HOME Monitoring Unit will be inspecting all of the 35 EHOP Agreement properties for both construction deficiencies and for violations of rental property standards. By the end of February 2008, every HOME project, originating in any of Housing Development's divisions, will be transferred to both the Occupancy Monitoring and SCEP's HOME Monitoring Units and scheduled for monitoring, as appropriate.

Finding 2: The Department's Loan Approval File Documentation Was Incomplete
LAHD Response

Comment 9

We agree with this finding for files initiated before 2006. In 2005, the Program Manager, responsible for the loan programs, implemented a standardized Single Family Rehabilitation Feasibility worksheet (in MS-Excel) that met all of the HOME requirements for eligibility and feasibility. The in-house Comprehensive Rehabilitation Programs staff and the CAs were trained in the system and it was updated and implemented in November 2005. In fixing the broken system, we moved forward with our improvements rather than trying to go back to mend older files.

Our review of the loan files showed that, for the in-house program and the CAs, all of the files, initiated in 2006, were in compliance with the eligibility[6] and property value analyses. The difference between LAHD's review and the OIG Representatives' review may be that LAHD counted files as complete, if a printout of the computerized home values (comparables) search (from Bank of America or other) was in the files. Even if the "as is property value" section of the Feasibility Worksheet was blank, the information was contained in the loan file. We do recognize the importance of filling out every portion of the form and have included that requirement in the Operations Manual.

Finding 2.1 Household Members Did Not Certify Zero Income

Comment 10

LAHD loan officers followed the procedures outlined in the Technical Guide for Determining Income and Allowances for the HOME Program for determining income eligibility. It does not appear that this Guide or Building HOME mention a certification of zero income. While we agree with the OIG Representative that we should add this requirement, we do not think that this should be a finding. The new Operations Manual does require that household members, who claim they have no income, sign a Certification Form stating that, under penalty of perjury, the property is their primary residence and that they have had zero income during the time period.

Finding 2.2 Property Values Were Not Fully Supported
LAHD Response

Comment 11

As discussed previously, many files audited by the OIG were originated in the period prior to 2006. We believe that a review of the files will show that all files, after November 2005, demonstrate how the estimated value was determined. Although staff did not note in writing why those properties were chosen as comparables. Speaking with the loan officers confirmed that there was a good reason for those choices (e.g., type of neighborhood, proximity to subject property) that the loan officer took into account.

[6] With the exception of the "zero income" certification.

Providing a written rationale for choosing comparables has been included as a requirement in the Operations Manual.

Finding 2.3 Loan Processing Times Were Often Excessive
We agree with this finding. There were approximately 160 open cases transferred to TSU when the reorganization of the Housing Department took place in 2005. Although it was designed to solve problems, the separation of the loan function from the construction function created a number of other problems. Loan officers felt separated from the rehab process and communication between the two units was strained. The TSU staff was overwhelmed by cases but the Loan Program finance officers continued to process applications (to show that they were doing their job). This resulted in exceedingly long loan processing and rehab construction times because the system was all backed up. Our understanding is that complaints about these problems were seen by the former, and now retired, Homeownership and Preservation Director as "personality conflicts" rather than as symptoms of very real problems that needed to be solved.

The Division did not meet its consolidated plan goals in 2004 because staff was relatively unsupervised in District offices and were not held to performance standards and production goals. Goals were not met in 2005 due to the problems described above. In 2006, management made the decision to scope down the amount of funds allocated to the rehab programs to fit production, while seeking a new Director and redeploying other staff to improve the program

After the current Director completed his assessment of the program, he recommended to senior management that the loan and construction staff be re-joined and placed under a Rehab Program Manager, reporting to him. Additionally, he established timeframes for each step of the rehab process and developed procedures requiring loan and construction staff to work together from the time a homeowner applies for assistance through close-out of the rehabilitation loan. These have been memorialized in the Operations Manual. Each project in the pipeline is reviewed on a bi-weekly basis by the team, supervisors and Rehab Program Manager in order to ensure it is moving along in a timely manner and problems are recognized and resolved (when more easily solved) before they become blockages.

Finding 2.4 Standard Policies and Procedures Were Not Maintained
While the Department did not have a standard set of written materials in the form of an Operations Manual, each loan officer and CA were given forms, formats, and checklists and training in addition to copies of the Technical Guide for Determining Income and Allowance in the HOME Program. We acknowledge the point made by the OIG Representative that a standardized Operations Manual and standard quality control activities in support of those policies and procedures are required. We do believe that the financial files initiated, after 2006, meet all of the HOME requirements.[7]

Finding 3: The Department's Status of Activities Was Not Reported to HUD in a Timely Manner
LAHD, like many large agencies, had multiple small databases that had been developed on an *ad hoc* basis to keep track of various types of projects and provide information for reports. None of the Department's project management databases were integrated with

[7] Except the no income certification.

IDIS or each other. This meant that the same project data was manually entered into several systems. In 2003, the Department, recognizing the importance of timely reporting and data entry into IDIS and the inefficiencies of the current systems, contracted with a Florida firm, Housing and Development Software (HDS), approved by HUD, to provide an off-the-shelf software package that would allow the Department to manage all its grant funds, and HUD projects and activities, and to automatically report activity data to IDIS. Although LAHD staff spent several years working with HDS to acquire and install this system, the system did not work as described. Ultimately, LAHD systems and management staff decided that further work with HDS would not achieve the goal of timely reporting and project tracking and terminated the contract in 2006.

Since then, LAHD Systems staff have initiated the in-house development of an interface with IDIS that will be user-friendly and collect all of the information required for sound project management and timely IDIS data entry and reporting. Various modules of the new Housing Information Management System (HIMS) have been rolled out during 2007 and the final module, which will integrate LAHD's data management with IDIS, is scheduled to be completed and installed during 2008.

Finding 3.1: Committed Funds and Completed Activities Were Reported Late
Finding 3.2: Procedures and Controls over Manual Data Entry Did Not Exist
As noted above, LAHD has focused on the development of the new data management system, and did not invest staff time in developing written procedures for the temporary requirement that data be entered directly into IDIS. Nevertheless, since this manual process has been necessary for longer than anticipated, we should have evaluated and documented the manual system and set timelines for each activity instead of only investing time in the new system to solve the problem. As a result of this audit, we are assessing the systems we are using right now and developing procedures and timelines for data entry at all phases. IDIS reports are now reviewed against reports from the "local" rehabilitation projects database. In addition, we are reviewing the processes and procedures for all of the LAHD units that implement and report HOME and CDBG-funded activities to ensure that their data entry and reporting into IDIS is timely. These performance measures will be incorporated into the new system as well.

Finding 3.3: HUD Relies on Timely Reporting
While we appreciate the point made by the OIG Representative regarding poor data reliability in HUD's online system, the LAHD has extensive controls within its current CBTS (Capital Budget Tracking System) to ensure that funds are spent appropriately. Staff focused on ensuring timely data entry into the CBTS to the detriment of our responsibilities for IDIS. Division management did not stress the importance of IDIS entry and timeliness, no written procedures were in place to guide this process and no quality control/supervisory practices were implemented to make sure that this happened.

Finding 4: The Department Improperly Allocated Administrative Costs to Projects
Finding 4.1: Soft Cost Allocation Formula Included Ineligible Expenses
All of the ineligible costs have been subtracted. Since Accounting works primarily with the HUD-approved City cost allocation system, it was natural to apply that methodology to determine soft costs. Accounting staff is now aware of the HOME requirements and that will not happen again.

Finding 4.2: Activity Accounts Did Not Directly Capture Staff Time
The Department now has a job costing system with written procedures in place to directly capture staff time spent on specific HOME program or other activities since Spring 2006. Since the rehabilitation programs have largely used CDBG funds since 2006, they have not had to use this system. It is standard practice for Major Projects staff who do work with the HOME program. In any event, staff have been trained in this system. Attachment A is a copy of an actual time sheet used to keep track of staff time for various projects.

Finding 4.3: Procedures to Cancel Activities Did Not Exist
These procedures have now been written down and reviewed by all appropriate staff. A routing checklist has been developed for all project files to ensure that the staff in various divisions who need the information in a timely manner will receive it and that items such as performance fees will be subtracted from HOME expenditures when projects are cancelled.

Finding 4.4: Administrative Costs Were Understated in HUD's Online System
The Department believes that we have fixed this problem and will work with HUD's Los Angeles CPD Office to ensure that this has been remedied and will not happen in the future.

Conclusion
Management and staff of the Los Angeles Housing Department appreciate the time taken by the OIG audit staff to conduct a thorough assessment, their willingness to discuss issues and to hear our point of view. As noted previously, the Department had identified many of these issues and begun to make improvements as early as 2005. Technical assistance from HUD to create written program operations manuals was requested in January 2006. Although that technical assistance was not forthcoming, staff worked to bring the program into compliance. Many improvements had not been finalized by the time the OIG audit was completed; the audit findings enriched the operations manuals that have now been developed. LAHD looks forward to working with HUD on these issues and demonstrating the improvements that have been instituted.

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Attachment A

City of Los Angeles

Time Sheet

Employee: [redacted]
Job Class: 1571-1 FINANCE DEV OFFICER I
Department: 3903-400 MAJOR PROJECTS
Pay Period: #13 12/09/2007 - 12/22/2007

Work Time Week 1

Variation Code	Work Order	Task	Sub Task	Sun	Mon	Tue	Wed	Thu	Fri	Sat	SH	BN	LV	Week1	Remarks
HW	3KD05068	000	000				1.00	1.00	1.00					3.00	Afton Place Apts.
HW	3KH09681	000	000		2.00		1.00	1.00	1.00					5.00	Mariposa Place
HW	3KD09788	000	000		2.00		1.00	1.00	1.00					5.00	Central Court
HW	3KD08912	000	000		2.00	1.00	1.00	2.00	1.00					7.00	Laguna Senior
HW	3KH08093	000	000		1.00	2.00	1.00	1.00	1.00					6.00	Vista Monterey
HW	3KH07635	000	000		2.00	2.00	1.00	1.00	1.00					7.00	Pico Gramercy
HW	3KD05053	000	000			2.00	1.00	1.00	1.00					5.00	L.A. Colorado
HW	3KDPA00C	000	000			2.00	2.00	1.00	1.00					6.00	Admin.
			Total	0.00	9.00	9.00	9.00	9.00	8.00	0.00				44.00	

Non-Work Time Week 1

Variation Code	Work Order	Task	Sub Task	Sun	Mon	Tue	Wed	Thu	Fri	Sat	SH	BN	LV	Week1	Remarks
				0.00	0.00	0.00	0.00	0.00	0.00	0.00				0.00	

Work Time Week 2

Variation Code	Work Order	Task	Sub Task	Sun	Mon	Tue	Wed	Thu	Fri	Sat	SH	BN	LV	Week2	Remarks
HW	3KD09068	000	000			1.00	1.00	1.00						3.00	Afton Place Apts.
HW	3KH09681	000	000			1.00	1.00	1.00	1.00					4.00	Mariposa Place
HW	3KD09788	000	000			1.00	1.00	1.00	1.00					4.00	Central Court
HW	3KD08912	000	000			1.00	1.00	1.00	1.00					4.00	Laguna Senior
HW	3KH08093	000	000			1.00			2.00					3.00	Vista Monterey
HW	3KH07635	000	000			2.00		1.00	1.00					4.00	Pico Gramercy
HW	3KD05053	000	000			1.00		2.00	1.00					4.00	L.A. Colorado
HW	3KDPA00C	000	000			1.00	1.00	2.00	2.00					6.00	Admin.
VC	3KDPA00C	000	000				4.00							4.00	Vacation
				0.00	0.00	9.00	9.00	9.00	9.00	0.00				36.00	

Non-Work Time Week 2

Variation Code	Work Order	Task	Sub Task	Sun	Mon	Tue	Wed	Thu	Fri	Sat	SH	BN	LV	Week2	Remarks
				0.00	0.00	0.00	0.00	0.00	0.00	0.00				0.00	

Grand Total

	Week 1	Week 2
Total Time	44.00	36.00

Submitted By: [redacted]
Submission Date: 12/19/2007 9:05:49 AM
Supervisor Signature: [redacted]
Approved
12/19/2007 12:17:01 PM

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OIG Evaluation of Auditee Comments

Comment 1 Although the Department's response contrasts the results of this OIG audit with the results of HUD's monitoring reviews performed by the program office, it is important to note that our review was a much more focused and in-depth review than HUD's routine monitoring could accomplish for such a large HOME program.

Comment 2 Our report acknowledged the Department's development of an on-line format that could serve as its local rehabilitation standards. However, during the audit, Department and contract agency officials did not convey the notion that all of the rehabilitation standards were documented in the on-line system used to prepare construction work write ups. Overall, finding one (inadequate construction monitoring) resulted from the Department's failure to maintain centralized, standard operating procedures for rehabilitation construction monitoring. Such procedures should reference where the required, written local rehabilitation standards are located/accessible. Further, because the HOME regulations require the participating jurisdiction to maintain local written standards for rehabilitation, the construction (TSU) supervisor should have known that the on-line version was to meet this requirement. Instead he provided us with an outdated written version. We agree that an on-line version is an acceptable format; however, we would expect the on-line version to be updated through a formal process that: documents effective dates, notifies customers of each new version and archives older versions. This is necessary to document applicable standards when disputes arise or compliance reviews are performed on projects contracted under the earlier versions. Without procedures that referenced the standards and a formal repository of older versions, we question whether the Department's on-line format was adequate to meet regulatory requirements at the time of our review.

Comment 3 We commend the Department for planning to identify and remedy rehabilitation construction deficiencies in HUD assisted properties beyond those identified in the audit.

Comment 4 The report states that $123,262 in HOME funds assisted noncompliant properties because this is the total amount disbursed for the cited properties. HOME regulations require that the entire property be rehabilitated to meet all applicable construction standards and, therefore, the entire amount is technically ineligible if any deficiencies are not corrected.

Comment 5 We commend the Department for its proactive approach to address this finding. In accordance with normal audit resolution procedures, the HUD program office will verify that any required corrective actions have been satisfactorily completed.

Comment 6 The Department's response fails to note the following limitations of the cited 2005 review. First, the review was an "Agreed Upon Review Procedures" and therefore would not address anything that was beyond the scope of the agreement, even if it were significant. Specifically, the report states: "The sufficiency of these procedures to evaluate and assess EHOP's compliance with its contractual obligations is solely the responsibility of HUD. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purposes for which this report has been requested or for any other purpose." Second, the stated purpose of the review was "to assist in evaluating the financial and program compliance of Enterprise Home Ownership Partners ("EHOP") relative to the future REO Acquisition Agreement between HUD, EHOP and the City of Los Angeles." There was no indication that the review considered applicable HOME program requirements, or included on-site property inspections.

Comment 7 In accordance with normal audit resolution procedures, the HUD program office will verify that any required corrective actions have been satisfactorily completed.

Comment 8 The Department did not provide us with documentation of final <u>comprehensive</u> inspections performed by LAHD staff for the two EHOP properties in our random sample.

Comment 9 We acknowledge that most files we reviewed included a Single Family Rehabilitation Feasibility worksheet and agree that this worksheet is a good tool to document eligibility determinations. Finding 2 resulted when we could not find adequate supporting documentation for the information and conclusions on the feasibility worksheets. As discussed in the report, our random sample found problems with support regarding determinations of zero income and how appraised values were determined. Some of the deficiencies we counted were for loan files approved in 2006. As noted in Appendix C Criteria, the HOME program regulations clearly require records demonstrating that the purchased price or estimated value after rehabilitation for each homeownership housing project does not exceed 95 percent of the median purchase price for the area in accordance with section92.254. *The records must demonstrate how the estimated value was determined.* (Italics added by OIG.)

Comment 10 We changed the subfinding section heading to read: "Documentation of Zero Income Was Inadequate." As discussed under comment 9, the overall finding 2 (incomplete loan approval file documentation) resulted because we consistently found minimal documented support for income and property eligibility determinations. Although we noted other weaknesses in income determinations, we were most concerned about a pattern of inadequate confirmation when the borrower claimed that extra (i.e. non borrower or spouse) adults with no income lived in the household. The response correctly notes that HUD's Technical Guide or <u>Building HOME</u> do not mention a certification of no income. Accordingly the operating policies and procedure that we recommend be developed for loan approvals could include an alternate method that would ensure claims of no income were reasonably supported.

Comment 11 See comment 9.

Appendix C

CRITERIA

<u>Finding 1</u>

HOME program regulations at

- 24 CFR [*Code of Federal Regulations*] 92.251(a)(1) require housing that is rehabilitated or constructed with HOME funds to meet all applicable local codes, rehabilitation standards, ordinances, and zoning ordinances at the time of project completion. The participating jurisdiction must have written standards for rehabilitation that ensure the HOME-assisted housing is decent, safe, and sanitary. Section 92.251(a)(2) requires that all other HOME-assisted housing (e.g., acquisition) meet all applicable state and local housing quality standards and code requirements, and if there are no such standards or code requirements, the housing must meet the housing quality standards in 24 CFR [*Code of Federal Regulations*] 982.401 (Section 8 Housing Quality Standards).

- 24 CFR [*Code of Federal Regulations*] 92.508(a)(3)(iv) require records that demonstrate that each project meets the property standards of section 92.251 and the lead-based paint requirements of section 92.355; and at Section (a)(6)(iii), require records documenting required inspections, monitoring reviews and audits, and the resolution of any findings or concerns.

- 24 CFR [*Code of Federal Regulations*] 92.602(a)(2) state that for rehabilitation that is completed in conjunction with the home purchase assisted with American Dream Downpayment Initiative funds, the rehabilitation assisted with American Dream Downpayment Initiative funds, including the reduction of lead paint hazards and the remediation of other home health hazards, must be completed within one year of the purchase of the home.

- 24 CFR [*Code of Federal Regulations*] 92.504(a) state that the participating jurisdiction is responsible for managing the day-to-day operations of its HOME program, ensuring that HOME funds are used in accordance with all program requirements and written agreements, and taking appropriate action when performance problems arise. The use of state recipients, subrecipients, or contractors does not relieve the participating jurisdiction of this responsibility. The performance of each contractor and subrecipient must be reviewed at least annually.

- 24 CFR [*Code of Federal Regulations*] 92.504(d)(1) state that during the period of affordability, the participating jurisdiction (the City) must perform on-site inspections of HOME-assisted rental housing to determine compliance with property standards of Section 92.251 no less than every three years for projects containing one to four units, every two years for projects containing 5 to 25 units, and every year for projects containing 26 or more units.

Office of Management and Budget regulations under 2 CFR [*Code of Federal Regulations*] Part 225 (previously OMB Circular A-87) require costs claimed under federal awards to be reasonable and adequately documented. In determining the reasonableness of a given cost, consideration shall be given to market prices for comparable goods and services.

Los Angeles Housing Department's Existing Housing Maintenance Code & Building Code Standards: LAMC Division 81 & 89 as amended, effective July 25, 1996.

Los Angeles Housing Department Housing Rehabilitation Standards (undated).

2002 City of Los Angeles Building Code Volume 1, based on 2001 California Building Code and the 1997 UBC.

2001 California Electrical Code, California Code of Regulations, Title 24, Part 3, effective November 1, 2002.

<u>Finding 2</u>

HOME program regulations at 24 CFR [*Code of Federal Regulations*] 92.508(a)(3)(v) require records demonstrating that each family is eligible in accordance with section 92.203 and at section (a)(3)(x), require records demonstrating that the purchase price or estimated value after rehabilitation for each homeownership housing project does not exceed 95 percent of the median purchase price for the area in accordance with section 92.254. The records must demonstrate how the estimated value was determined.

<u>Finding 3</u>

HOME program regulations at

- 24 CFR [*Code of Federal Regulations*] 92.500(d)(1) state that HUD will reduce or recapture the amount of HOME funds that was either not committed within 24 months or was not expended within five years after the funding agreement.

- 24 CFR [*Code of Federal Regulations*] 92.502 require that complete project completion information be entered into the HUD's online system within 120 days of the project's final disbursement.

HUD's guidance in the Office of Community Planning and Development's Notice 01-13 states that information in HUD's Integrated Disbursement Information System is used to determine compliance with these deadlines on an annual, cumulative basis.

HUD guidance in <u>Building HOME</u>, April 2002, states that grantees should update HUD's online system information quarterly.

Finding 4

HOME program regulations at

- 24 CFR [*Code of Federal Regulations*] 92.207 cap expenditures for reasonable administrative and planning costs at 10 percent of the annual HOME grant.

- 24 CFR [*Code of Federal Regulations*] 92.250(a) limit the total amount of HOME funds that can be charged per unit to each rehabilitation activity.

- 24 CFR [*Code of Federal Regulations*] 92.206(d) state that eligible project costs include other reasonable and necessary costs incurred and associated with the financing or development (related soft costs) of housing assisted with HOME funds.

- 24 CFR [*Code of Federal Regulations*] 92.205(e) state that a HOME-assisted project that is terminated before completion, either voluntarily or otherwise, constitutes an ineligible activity, and any HOME funds invested in the project must be repaid.

Guidance in the Office of Community Planning and Development's Notice 06-01, dated February 1, 2006, states that costs that are shared among several departments are always administrative costs as opposed to project costs.

Appendix D

SCHEDULE OF ACTIVITIES SAMPLED

HUD activity number	Amount committed	Rehabilitation loan type[18]
7825	$39,814	Rehabilitation - Department
7847	$239,440	Enterprise
7929	$105,000	Enterprise
8203	$52,371	Rehabilitation - contract agency
8257	$21,045	Rehabilitation - Department
8300	$51,775	Rehabilitation - contract agency
8415	$66,895	Purchase and rehabilitate
8515	$57,985	Rehabilitation - contract agency
8565	$16,000	Rehabilitation - Department
8903	$150,000	Rehabilitation - Department
8939	$58,417	Rehabilitation - contract agency
8945	$76,880	Rehabilitation - contract agency
8959	$68,500	Rehabilitation - contract agency
9179	$38,000	Rehabilitation - contract agency
9518	$117,818	Purchase and rehabilitate
9622	$204,000	Rehabilitation - Department
9744	$4,420	Rehabilitation - contract agency
9765	$28,970	Rehabilitation - Department
9796	$104,700	Purchase and rehabilitate
9949	$111,125	Purchase and rehabilitate
9992	$108,000	Purchase and rehabilitate
10063	$115,000	Purchase and rehabilitate
10067	$118,000	Rehabilitation - contract agency
10087	$137,716	Rehabilitation - contract agency
10117	$115,000	Purchase and rehabilitate
10142	$135,000	Rehabilitation - Department
10170	$105,000	Purchase and rehabilitate
Total	**$2,446,870**	

Source: HUD Integrated Disbursement Information System and loan agreements

[18] Rehabilitation – Department loans were underwritten and monitored by officials in the Preservation Unit; Rehabilitation – contract agency loans were underwritten and monitored by one of four contract agencies; Purchase and rehabilitate loans were underwritten by officials in the Homeownership Unit; and Enterprise loans were rehabilitation loans made to a developer.

Appendix E

SCHEDULE OF DISBURSEMENTS FOR PROPERTIES REHABILITATED BY ENTERPRISE

HUD activity number	Date committed	Activity status	Status date	Amount disbursed
6831	July 12, 2002	Complete	July 11, 2004	$130,837
6832	July 12, 2002	Complete	July 12, 2003	$149,925
6833	July 12, 2002	Complete	July 12, 2003	$93,420
6834	July 12, 2002	Complete	July 12, 2003	$114,135
6835	July 12, 2002	Complete	July 12, 2003	$56,865
6836	July 12, 2002	Complete	July 12, 2003	$115,580
7782	Aug 5, 2003	Complete	Aug 6, 2003	$106,646
7783	Aug 5, 2003	Complete	Aug 6, 2003	$129,123
7784	Aug 5, 2003	Complete	Aug 6, 2003	$166,609
7785	Sep 16, 2003	Complete	Sep 18, 2003	$62,698
7786	Aug 5, 2003	Complete	Aug 6, 2003	$106,975
7841	Apr 2, 2004	Complete	Apr 12, 2004	$234,664
7849	Apr 1, 2004	Complete	Apr 5, 2004	$150,000
7851	Nov 19, 2003	Complete	Nov 20, 2003	$100,214
7853	Nov 19, 2003	Complete	Nov 20, 2005	$210,575
7854	Nov 14, 2003	Complete	Nov 15, 2003	$140,000
7855	Nov 14, 2003	Complete	Nov 15, 2003	$105,000
7856	Nov 14, 2003	Complete	Nov 15, 2003	$88,085
7857	Nov 14, 2003	Complete	Nov 15, 2003	$105,000
7921	Nov 14, 2003	Complete	Nov 16, 2003	$117,738
7922	Nov 19, 2003	Complete	Nov 24, 2003	$219,705
7928	Nov 19, 2003	Complete	Nov 28, 2003	$114,000
8140	Sep 17, 2003	Complete	Sep 20, 2004	$172,768
8324	Apr 2, 2004	Complete	Mar 4, 2005	$205,457
8327	Dec 29, 2003	Complete	Dec 28, 2004	$84,764
8328	Apr 8, 2004	Complete	May 8, 2004	$212,291
8329	Dec 22, 2003	Complete	Nov 22, 2004	$105,000
8330	Jan 12, 2004	Complete	Nov 12, 2004	$167,573
8331	Mar 16, 2004	Complete	June 16, 2004	$189,953
8332	Apr 8, 2004	Complete	Aug 4, 2004	$174,486

HUD activity number	Date committed	Activity status	Status date	Amount disbursed
8333	Dec 22, 2003	Complete	June 23, 2005	$105,000
8334	Dec 22, 2003	Complete	Nov 11, 2004	$107,889
8335	Dec 29, 2003	Complete	Feb 27, 2004	$140,000
8403	Apr 22, 2004	Complete	May 22, 2004	$199,758
8543	May 12, 2004	Complete	May 12, 2005	$201,977
Total (2 pages)				**$4,884,710**

Source: HUD Integrated Disbursement Information System