audit report

Issue Date September 22, 2009	
Audit Report Number 2009-KC-1010	

TO: Frances M. Cleary, Deputy Director, Office of Public Housing, 7APH

//signed//

FROM: Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

SUBJECT: The Kansas City, Kansas, Housing Authority Inappropriately Spent Federal Funds for Nonfederal Development Activities

HIGHLIGHTS

What We Audited and Why

We reviewed the development activities of the Kansas City, Kansas, Housing Authority (Authority) to determine whether the Authority improperly spent federal public housing funds when developing and operating nonfederal developments. We conducted the audit because of a citizen complaint received by our office.

What We Found

The Authority inappropriately spent federal funds for nonfederal development activities. It transferred nearly $1 million from its public housing general fund bank account to the Community Housing Investment Group's (the Authority's nonprofit affiliate) bank account between January 2002 and December 2006. It also inappropriately spent federal funds for payroll costs when staff worked on nonfederal development activities. None of the nonfederal developments that staff worked on were projects covered by the annual contributions contract, nor had HUD approved the use of public housing funds for these activities.

What We Recommend

We recommend that HUD require the Authority to repay its public housing program nearly $184,000 from nonfederal sources for federal funds that were inappropriately used and not yet repaid and to implement adequate procedures to ensure that it does not spend HUD assets on nonfederal activities without HUD approval. Additionally, HUD should require the Authority to provide documentation to support payroll costs allocated to HUD programs or reimburse its HUD programs from nonfederal sources for costs that it cannot adequately support. HUD should also require the Authority to implement an acceptable method for allocating future payroll costs.

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

Auditee's Response

The Authority generally agreed with our conclusions and recommendations but disagreed with our calculation of questioned payroll costs. We provided the draft report to the Authority on August 20, 2009, and requested a response by September 11, 2009. It provided written comments on September 11, 2009.

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

TABLE OF CONTENTS

Background and Objective 4

Results of Audit

Finding 1: The Authority Inappropriately Spent Federal Funds for Nonfederal Development Activities 6

Finding 2: The Authority Inappropriately Spent Federal Funds for Payroll Costs When Staff Worked on Nonfederal Development Activities 9

Scope and Methodology 12

Internal Controls 13

Appendixes

A. Schedule of Questioned Costs and Funds to Be Put to Better Use 15

B. Auditee Comments and OIG's Evaluation 16

BACKGROUND AND OBJECTIVE

The Kansas City, Kansas, Housing Authority (Authority) was chartered by the State of Kansas in 1957. The Authority's mission is to help families and individuals with low and moderate incomes by providing safe, affordable, quality housing; partnering with community services and agencies; and promoting economic opportunity. The Authority is governed by a 12-member board of commissioners that provides oversight to the agency and its staff.

The Authority owns and operates 2,045 public housing units that provide housing options for the disabled, elderly, and families whose income meets U.S. Department of Housing and Urban Development (HUD) guidelines. The Authority also administers a Section 8 Housing Choice Voucher program that enables 1,469 low-income families to rent from a private landlord with rental assistance administered by the Authority. The Authority received $6.2 million for its public housing program and $8.4 million for its Section 8 program for fiscal year 2008.

To participate in HUD's public housing programs, the Authority executed an annual contributions contract with HUD on January 23, 1996. The annual contributions contract defines the terms and conditions under which the Authority agreed to develop and operate all projects under the agreement. The contract defines a project as any public housing developed, acquired, or assisted by HUD under the United States Housing Act of 1937, as amended. The contract states that the Authority may withdraw public housing funds only for the payment of the costs of development and operation of the projects under the contract or other purposes approved by HUD.

Due to concerns about housing authority development activities nationwide, on June 20, 2007, HUD's Office of Public and Indian Housing (PIH) issued Notice PIH 2007-15 (HA), "Applicability of Public Housing Development Requirements to Transactions between Public Housing Agencies and their Related Affiliates and Instrumentalities." This notice reaffirmed the requirements of public and Indian housing programs, including the annual contributions contract, that apply to public housing development activities.

In accordance with its agency plan, a public housing agency may form and operate wholly owned or controlled subsidiaries or other affiliates. Such wholly owned or controlled subsidiaries or other affiliates may be directed, managed, or controlled by the same persons who constitute the board of directors or similar governing body of the public housing agency or who serve as employees or staff of the public housing agency but remain subject to other provision of law and conflict-of-interest requirements. Further, a public housing agency, in accordance with its agency plan, may enter into joint ventures, partnerships, or other business arrangements with or contract with any person, organization, entity, or governmental unit with respect to the administration of the programs of the public housing agency such as developing housing or providing supportive/social services subject to either Title I of the United States Housing Act of 1937, as amended, or state law.

The Authority set up a nonprofit affiliate, Community Housing Investment Group, in 2001 so the Authority could develop mixed-financed properties to create new public housing for low-income families. The Authority's board of commissioners' chairman and the executive director sit on the board of directors for the nonprofit affiliate. The nonprofit affiliate tried to develop four different projects, but only Delaware Highlands Assisted Living was completed.

Delaware Highlands Assisted Living

Delaware Highlands Assisted Living is a 121-unit property that began development in 2003 and opened in September 2006. It was not constructed using mixed financing, nor does it contain public housing units. The Authority's executive director has managed the daily operations of the property since September 2008.

Our audit objective was to determine whether the Authority improperly spent federal public housing funds when developing and operating nonfederal developments.

RESULTS OF AUDIT

Finding 1: The Authority Inappropriately Spent Federal Funds for Nonfederal Development Activities

The Authority inappropriately spent federal funds for nonfederal development activities. This condition occurred because the executive director relied on consultants, who told him it was acceptable to spend public housing funds on nonfederal development and repay the funds when permanent financing was in place. As a result, the Authority did not have nearly $1 million of its public housing funds available for the intended purpose, which was to provide decent and safe housing for low-income families, the elderly, and persons with disabilities.

Authority Used Public Housing Funds to Pay Nonfederal Development Expenses

The Authority inappropriately spent HUD public housing funds for nonfederal development activities. According to the Authority's annual contributions contract with HUD, the Authority may withdraw money from its public housing fund only for the payment of the costs and operation of the projects covered under the contract. The nonfederal developments were not approved projects under the contract.

The Authority transferred nearly $1 million from its public housing general fund bank account to the Community Housing Investment Group's (the Authority's nonprofit affiliate) bank account between January 2002 and December 2006. In addition to the transfers, the Authority wrote a $500 check from its public housing general fund account for an application to the Internal Revenue Service for nonprofit status on behalf of the nonprofit affiliate. When the nonprofit affiliate received bond sale proceeds and construction loans in March 2005, it repaid the Authority nearly $803,000 but later used another $23,000 in federal funds. The nonprofit affiliate still owed about $184,000 to the public housing general fund as of May 2009.

Calendar year	Public housing funds used	Balance
2002 (includes $500 check)	$163,367	$163,367
2003	$81,832	$245,199
2004	$676,262	$921,461
2005 (January through March)	$42,349	$963,810
2005 (March repayment)	($802,835)	$160,975
2005 (April through December)	$5,272	$166,247
2006	$17,654	$183,901

The nonprofit affiliate used the inappropriately transferred money to pay predevelopment costs for two planned developments. Only one of the two planned developments materialized, Delaware Highlands Assisted Living. The predevelopment expenses included the land purchase for Delaware Highlands Assisted Living and fees for attorneys, architects, and appraisers.

Executive Director Relied on Consultants

The executive director relied on consultants, who told him it was acceptable to spend public housing funds on nonfederal development and repay the funds when permanent financing was in place. The executive director stated that the consultants told him the Authority could use the HUD funds as long as the Authority accounted for and repaid the funds when it obtained other sources of financing. The executive director relied on this information and presented it in the same way to the Authority's board of commissioners. The commissioners also relied on this advice.

In addition, the executive director told us that the Authority's independent auditor did not consider the debt owed by the nonprofit affiliate to the Authority to be a reportable finding. He told us that because the consultants and the independent auditor thought this practice was acceptable, he relied on their advice as experts in their respective fields.

Public Housing Funds Were Not Available for Intended Purposes

Beginning in 2002 and continuing through May 2009, the Authority had not had nearly $1 million of its public housing funds available for the intended purpose, which was to provide decent and safe housing for low-income families, the elderly, and persons with disabilities.

In addition, as of May 2009, the nonprofit affiliate owed the Authority about $184,000, with no apparent ability to repay the funds until the Delaware Highlands Assisted Living facility generates sufficient funds to begin repayment. The facility's audited financial information, for the period ending December 31, 2008, showed that the facility had an operating loss of nearly $1 million since it opened in September 2006. Therefore, persons intended to benefit from the public housing funds will receive less assistance than they would have until the Authority secures funds to repay the public housing program.

Recommendations

We recommend that the Deputy Director, Office of Public Housing, require the Authority to

1A. Repay its public housing program from nonfederal sources for any federal funds inappropriately used, including $183,901 owed by the Community Housing Investment Group as of March 31, 2009.

1B. Implement adequate procedures to ensure that it does not spend HUD funds on nonfederal programs and activities without HUD approval. These procedures should include following Notice PIH 2007-15, which addresses spending HUD-related assets in relation to development activities.

Finding 2: The Authority Inappropriately Spent Federal Funds for Payroll Costs When Staff Worked on Nonfederal Development Activities

The Authority inappropriately spent federal funds for payroll costs when staff worked on nonfederal development activities. This condition occurred because the Authority's executive director did not understand the requirements. As a result, public housing tenants did not receive the full benefit of Authority employees' time and efforts for which the Authority paid nearly $1.5 million in payroll costs.

Authority Spent Federal Funds on Nonfederal Activities

The Authority inappropriately paid payroll costs (salaries and benefits) from its federal public housing funds for staff that worked on nonfederal development activities. The annual contributions contract between the Authority and HUD allows the Authority to use public housing funds only for the costs of development and operation of the projects under the contract or other purposes approved by HUD. None of the nonfederal developments that staff worked on beginning in January 2002 was covered by the annual contributions contract, nor had HUD approved the use of public housing funds for payroll costs when staff worked on these nonfederal efforts.

Five Authority employees spent a portion of their time working on nonfederal development activities beginning in January 2002. Beginning in January 2003, staff worked on developing Delaware Highlands Assisted Living, a nonfederal development, which opened in September 2006. After the facility opened, two additional staff members began spending time on nonfederal activities.

Authority Did Not Track Time for Nonfederal Activities

Authority staff that worked on nonfederal development activities did not track their time spent on federal or nonfederal activities. The annual contributions contract requires the Authority to maintain records that identify the source and use of funds in a way that allows HUD to determine that all funds are and have been spent in accordance with each specific program requirement. Further, Office of Management and Budget Circular A-87 states that when employees work on multiple activities, the employer must support salary distributions with personnel activity reports or equivalent documentation.

The executive director and department heads were primarily the employees who worked on nonfederal development activities. The Authority did not require its managers to keep detailed records of their activities. As a result, the Authority had no records of staff time spent on federal or nonfederal activities and, therefore, could not support payroll costs charged to the public housing program during the nonfederal development period.

In addition, the Authority's executive director began managing the daily operations of Delaware Highlands Assisted Living in September 2008. The nonfederal development had incurred losses of nearly $1 million since opening in 2006. The nonprofit affiliate's board members fired three management agents during this period. As a result, the nonprofit affiliate's board members instructed the executive director to manage Delaware Highland Assisted Living's daily operations in an attempt to make the nonfederal development profitable. The executive director told us that he expected to manage the nonfederal development for at least the next year.

Authority Management Did Not Understand Requirements

The executive director did not understand HUD requirements. He believed that it was the Authority's responsibility to pay salaries for Authority staff working on nonfederal developments because the board of commissioners instructed him to carry out the development activities.

The board of commissioners

- Created a nonprofit to develop low-income housing,
- Appointed the executive director as a member of the nonprofit board, and
- Expected the executive director to aggressively pursue developing low-income housing.

The executive director told us that he believed it was his responsibility to carry out the board of commissioners' wishes and in hindsight he should have kept track of the time he and other staff spent on the nonfederal activities. He also told us that he tried to work on the nonfederal activities outside the normal 40-hour work week but had no documentation to support this assertion. In addition, he told us that he tried to limit the amount of time his staff spent on the nonfederal development activities.

Authority Tenants May Have Been Underserved

Public housing tenants did not receive the full benefit of Authority employees' time and efforts for which the Authority paid nearly $1.5 million in payroll costs.

Further, without an acceptable method of allocating such costs, the Authority will pay at least $194,000 in unsupported payroll costs, excluding benefits, from federal funds within the next year. When the Authority used federal funds to pay for employee time spent on activities other than public housing activities, it deprived the Authority's public housing tenants of funds that should have been spent on their needs.

Recommendations

We recommend that the Deputy Director, Office of Public Housing, require the Authority to

2A. Provide documentation to support payroll costs allocated to HUD programs or reimburse its HUD programs from nonfederal sources for costs that it cannot adequately support. These costs should include $1,452,462 allocated from April 1, 2002, to March 31, 2009.

2B. Implement an acceptable method for allocating future payroll costs, such as daily activity reports or equivalent documentation, for services performed. This measure will ensure that an estimated $194,079 in payroll costs that will be allocated in the next year will be put to better use.

SCOPE AND METHODOLOGY

Our review generally covered the period January 2002 through February 2009 and was expanded as necessary. We performed on-site work from March through July 2009 at the Authority's office located at 1124 North 9th Street, Kansas City, Kansas.

To achieve our audit objective, we conducted interviews of the Authority's staff and members of its board of commissioners. We also conducted interviews of HUD staff at the Kansas City, Kansas, Office of Public Housing. We reviewed the Authority's policies and procedures, development files, general ledgers, payable files, payroll files, and audited financial statements. We also reviewed the Authority's annual plan, board of commissioners meeting minutes, correspondence with HUD, annual contributions contracts, bank statements, and bank loan documents. In addition, we reviewed federal regulations and HUD requirements.

We reviewed reports generated from the Authority's computerized accounting system for evidence of spending public housing assets without prior HUD approval. We used the computerized data for background information purposes only; therefore, we did not conduct tests of the data or controls governing the data. We did not use the data to support audit conclusions but used only original source documents to reach our conclusions.

We assigned a value to the potential savings to the Authority if HUD implements our recommendations. If HUD implements recommendation 2B requiring the Authority to implement an acceptable method for allocating future payroll costs, it will protect an estimated $194,079 in salaries for staff who will likely work on nonfederal development activities in the next fiscal year. The estimate will be a recurring benefit; however, our estimate reflects only the initial year of this benefit.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

INTERNAL CONTROLS

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

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

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

Relevant Internal Controls

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

- Controls to ensure that the Authority complied with its annual contributions contract with HUD regarding the use of federal funds.

- Controls to ensure that the Authority complied with Office of Management and Budget Circular A-87, "Cost Principles for State, Local, and Indian Tribal Governments," regarding support for payroll costs and funding sources used for these costs.

- Controls to ensure adequate oversight of the Authority's daily operations.

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 Weakness

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

- The Authority did not have adequate controls in place to ensure that its spending of federal funds complied with federal regulations and its annual contributions contract with HUD (findings 1 and 2).

Separate Communication of Minor Deficiencies

We reported a minor internal control issue to the auditee in a separate memorandum, dated September 8, 2009.

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1A	$183,901		
2A		$1,452,462	
2B			$194,079

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

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

3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest,-costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified.

If HUD requires the Authority to implement an acceptable method for allocating future payroll costs, it will protect future payroll costs for staff that will likely work on nonfederal development activities in the next fiscal year. The estimate will be a recurring benefit; however, our estimate reflects only the initial year of this benefit.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Kansas City, Kansas Housing Authority
1124 North Ninth Street
Kansas City, Kansas 66101-2197
(913) 281-3300 FAX (913) 279-3428
www.kckha.org

September 11, 2009

Mr. Ronald J. Hosking
U.S. Dept. of HUD
Office of the Inspector General for Audit
400 State Ave.
Kansas City, KS 66101

RE: HUD IG Audit 2009 Development Activities

Dear Mr. Hasking:

This transmits my response to the IG audit findings.

Best regards,

Thomas W. Stibal
Executive Director

TWS/jr

Comment 1

Memorandum

To: Ronald J. Hosking
HUD office of Inspector General for Audit

From: Thomas W. Stibal
Executive Director, KCKHA

Date: September 8, 2009

Subject: HUD IG Audit 2009, Development Activities

Background

The Housing Authority of Kansas City, Kansas (KCKHA) became interested in potential development, initially in conjunction of the HOPE VI program, as a tool to redevelop our Juniper Gardens development, and then even more so after the passage of QHWRA in 1996, which seemed to impose upon housing authorities the obligation to seek and explore any development and redevelopment opportunities that were presented in their respective communities. KCKHA had no staff or board members that had participated in development in this setting. After staff submitted multiple HOPE VI applications that were not funded, the board advocated for the procurement of consultants to provide experience, expertise, and to spear head development initiatives for KCKHA.

HUD did not have a PIH notice regarding development activities published at the time, which provides PHA's and consultant's guidance on the departments interpretation of the language of the CFR's. As pointed out by IG Audit 2004-AT-0001,PIH notice 91-39 was allowed to expire in 1992, and no new notices were published to replace PIH notice 91-39, nor were any PIH notices published following the passage of QHWRA in 1996. In fact PIH notice 2007-15 is the first guidance we have seen offered on HUD's interpretation of the development rules, other than the 2004-AT-0001 audit report. It is also important to note that audit report 2004-AT-0001 recognized that consultant's giving advice and advice be given at conferences may be incorrect. It stated: "We are concerned that PHAs have received improper guidance on how to develop housing at these conferences."

KCKHA did hire consultants in 2000. They were chosen after a procurement process that evaluated candidates based upon their expertise, experience, and integrity. A committee of board members, staff, a representative of the Mayor's office, a representative of the local HUD field office, a representative of LISC, and two representatives of Fannie Mae graded and interviewed the proposers. [redacted] was the successful candidate. We also requested that legal advice be provided as part of the proposal for services, and [redacted] of

1

**We redacted names to protect the individual's or entity's privacy.

[redacted] provided legal advice. Additionally we had procured [redacted] a local bond attorney to provide financing advice. Our staff counsel was not available from October of 2001 to September of 2003, as he was called up for military duty following 9/11.

Following the consultant's advice KCKHA developed an integrated multi deal development strategy, and we visited with the HUD office of public housing investments in February of 2001, at which time we outlined our overall development strategy and discussed the two first mixed finance development proposals. We subsequently, initiated participation in two mixed finance development projects, which, it is my understanding were undertaken correctly and are not at issue here.

In 2002, also following consultant's advice we undertook the development of an assisted living facility, which was a badly needed facility in this community. We believed that a large part of the target market would be public housing residents who were over eighty years old and who were having difficulty living independently in our public housing program. We initially tried to do this at the old Bethany hospital, as an adaptive reuse, but could not make that work financially, so we ended up with a new site and development called Delaware Highlands Assisted Living, LLC. (DHAL). All residents of DHAL are residents who qualify financially for federal housing assistance and, since opening in September of 2006, over 95% of residents income is less than 50% of AMI, with the other 5% at or below 60% AMI. All residents meet low or very low income restrictions, and all are frail elderly. This development has allowed us to serve residents that are eligible for federal housing assistance without HUD or KCKHA needing to make a ten million dollar capital investment to build the facility.

Comment 1

Comment 2

Comment 3

During the course of this audit we have been advised that this effort to develop an assisted living facility was not done correctly. [redacted] our consultants, indicated that the advice given to KCKHA "was based on circumstances and practices and interpretation of legitimate funds use for 'affordable housing purposes' before the HUG IG report was issued." They did advise KCKHA in November of 2004, that "predevelopment costs covered by (CHIG's (Community Housing Investment Group, the PHA non profit affiliate) investment, for which funds were borrowed from the Housing Authority, will be refunded at closing. This is necessary due to a change in HUD guidelines per a January 2004 report published by HUD's Inspector General pertaining to the nature of PHA financial involvement in other housing initiatives, notably relative to the nature of funds used and applicable Federal regulations". As a result of this advice funds used for predevelopment costs of Delaware Highlands were repaid to KCKHA at the financial closing. There were also some predevelopment funds expended earlier when we attempted to first do an assisted living facility as an adaptive reuse of an existing hospital. This occurred in 2002, well before the 2004 IG audit report was issued that changed the advice given us by our consultants. We have not had available non Federal funds to repay, those costs related to the Bethany Hospital site, and could not include them in project costs for DHAL for reimbursement in March of 2005.

Comment 4

I would also like to point out that KCKHA has reported all of the development activities it engaged in from 2002 to 2008 in its annual plan, and those plans were all approved by HUD. In fact KCKHA told HUD it was engaged in these development activities over 25 times in its annual plan submissions from 2002 to 2008. PHA's advising HUD of their planned development activities in their annual plan submissions was one of the recommendations of IG audit 2004-AT-0001. Our understanding of the purpose of the plans was to give HUD the opportunity to review PHA activities and question or provide guidance to PHA's prior to them engaging in the activities. All plans were approved as submitted.

Finding No. 1.

Comment 5

Although we believe that we made every effort to follow HUD rules and guidelines regarding development activities we do agree that the KCKHA affiliate owes the KCKHA 183,901 dollars, and agree with the numbers reflected in the chart on page seven of the report.. This number has been reported accurately to HUD over the course of the period currently being audited in our annual audits and financial statements since 2002. All of which were approved by HUD.

Comment 6

We believe that the conclusion of the IG audit that "Beginning in 2002 and continuing through May 2009, the Authority had not had nearly $1 million of its public housing funds available for the intended purpose," overstates the unavailability of funds to the public housing agency, as that amount was tied up for only about an eight month window of time. The balance of the time the amount was under $250,000. And we agree with the HUD Office of Public Housing Investment, which in its response to IG Audit 2004-AT 0001 stated that there is only "true risk if a "PHA becomes financially distressed". KCKHA is not financially distressed, nor were any management decisions regarding operations or capital investments decisions impacted by these development activities.

Finally, we acknowledge that DHAL had initial operational problems during its first two years of operations, but since the developers established a management entity in September of 2008, the operation has stabilized and become predictable, and begun to cash flow, although still under performing its predevelopment pro forma. As of July 31, 2009, according to the financial statements prepared by Keller and Owen the CPA firm that provides the accounting services to DHAL, the project was cash flowing year to date. DHAL was also appraised in March of 2009, and it appraised for $10,050,000 and has a bond balance of $6,630,000, so there is about $3,420,000 in equity in the project. CHIG's interest of two thirds ownership we believe protects KCKHA's interest. KCKHA does not believe that its obligation due from CHIG will not be met.

Comment 7

Finding 2.

After reviewing OMB circular A-87, we agree that CHIG may owe KCKHA money for reimbursement of salaries, but we believe the $1.5 million identified is an overstatement of the amount and that it is much smaller. The current IG audit identified five employees who may have worked for the benefit of either CHIG, the affiliate, or DHAL. They are the executive assistant, the elderly services coordinator, the director of finance, the modernization coordinator, and the executive director.

Additionally, the auditor found that two bus drivers' wages should be reimbursed. KCKHA was billing DHAL for expenses for the bus service, but not wages. This was the result of miscommunication within the agency, and staff has been instructed to back bill the wages and to bill for wages and expenses in the future. This is about a four thousand dollar portion of the total payroll amount noted by the IG auditor.

The executive assistant's entire salary for a five year period was included in the amount cited by the IG auditor. In fact the executive assistant was given one task to do and that was to help prepare a list of invitees to the grand opening of DHAL. She was given that task so that we were sure to include invitations to HUD, current and former KCKHA commissioners, and others in the community with whom KCKHA had working relationships. This task took place in 2006, and required about 3 hours of her time. One can certainly make the case that KCKHA benefitted from that work and our community relationships improved by the recognition received during the grand opening. Other than that she has been given no tasks related to the development or operation of DHAL. Neither she nor I can say that she did not handle occasional phone calls that came to KCKHA's switchboard or mail that came to KCKHA's mailing address, but that is certainly minimal involvement, and really no different that redirecting calls that come to KCKHA that were meant to go to HUD or other departments of the city, or redirecting mail that came to KCKHA that was not addressed to us. This employee spent about 3 of 12,480 hours over the five year period on this task she was asked to complete, about 0.026 % of her time.

The elderly services coordinator entire salary was included for a two year period, 2008 and 2006. In 2008 she was tasked with filing a report with the state of Kansas. A review of her calendar showed that she worked about 5.5 hours on that project. That was her only task related to the DHAL development or operation during 2008. The auditor also included her salary for 2005, but that may have been meant to be 2006. In 2006, as elderly services coordinator she set up meetings with the marketing persons from DHAL and the resident associations in our high rises. This we would characterize as part of her job description at KCKHA, and not marketing DHAL as characterized by the IG auditor. The elderly services coordinator regularly set up speakers and presentations for our elderly residents, and helped them identify services in the community to help them remain independent. As elderly services coordinator, she also was tasked with identifying persons who were no longer able to live independently and either to help them find new accommodations or to recommend that their lease be terminated, as they began to pose a risk to themselves or others. Clearly, coordinating information about an affordable assisted living facility was providing a benefit to those public housing residents who had reached an age that they could no longer live independently, and was a function of her position at KCKHA and not marketing for DHAL. A review of her calendar showed about 14 hours engaged in this activity in 2006. In this case KCKHA believes that this employee spent about 5.5 hours of 4160 hours of her time or 0.12% of her time on tasks assigned for DHAL.

The third employee was the director of finance. His entire salary for a three year period was included. During 2003 he completed 21 banking transactions, during 2004 he completed 43 banking transactions and during 2005 he completed 14 transactions, for a total of 82 transactions over the three year period. Allowing 30 minutes per transaction the time believed to be used by this employee is 41 hours. This employee also met with the consultants when they were in town on a monthly basis in 2003, 2004 and 2005 until the financing closed. Once construction started in March of 2005 he was no longer involved. In this case KCKHA believes that the employee used about 68 hours of a total of 6240 hours during the three year period, about 1.0 percent of his time.

The fourth employee was the modernization coordinator. His entire salary was included for a period of five years by the IG auditor. Because this was a construction project he was the logical staff person to have involved.

A. His job during construction his tasks were: 1. To participate in the owner and bank inspections that took place once a month from April of 2005 to September of 2006, a period of 18 months, . These inspections took about 2 hours. 2. To help process the request for payment and to keep files of the records for the project. This task took about another two hours per month. He did not do other inspections as the bank and owner had a construction inspector that worked with the project architect during the course of the month, and who approved the construction draw prior to the inspection being performed. For this time frame of the work KCKHA believes that he spent about 72 hours of 3120 hours, or about 2.0% of his time.

B. After the facility opened he was charged with maintaining the checkbook, registers and bank statement files. He was also charged with maintaining the files for the pay and reimbursement requests of the management company. He also met monthly with the development group when the checks were prepared for the management company. This time frame was from October 2006 to May 2007 about 1400 working hours. We believe that the time spent was about 48 hours or 3.0% of his time. Additionally at year end the books provided by the management company contained errors and he spent about an additional 8 hours helping to provide more accurate year end financials.

C. From June of 2007 to December 2007 he continued to maintain the check registers and files for payment requests, but was relieved of the responsibility of meeting with the development team to process checks for payments and reimbursements. KCKHA believes that his time spent on this activity was about 21 hours of the approximately 1200 hours he spent working or about 2% of his time.

D. From January to October of 2008 he continued to maintain check registers and files with payment requests. We believe that his time spent was about 30 hours of the 1730 hours he would have worked during that time, or about 2% of his time. During this time he also spent about 6 hours helping to clarify year end statements.

E. From October of 2008 until September of 2009 the modernization coordinator served as custodian of the bank statements. We believe that he spends about 30 minutes per month filing bank statements and scanning them and distributing them via email to the parties on the distribution list. During this time frame this employee spent 6 hours helping fill out an annual report, and about 4 hours helping to clarify year end statements in January of 2009. This employee spent 16 of 2080 hours on DHAL related work or about or about 0.6% of his time.

The modernization coordinator is participating in a time study along with the executive director to objectively demonstrate time spent at the suggestion of the IG auditor. We began the time study in July, and will continue to the end of the year.

The final employee determined by the IG Auditor is the executive director, and his entire salary was included for the entire seven year period of the audit. He was the only employee involved from the beginning of this development to the end of it. The executive director did not keep track of time during this process because the work that he does for CHIG and DHAL is community service. CHIG is a not for profit corporation in Kansas, and in order for it to maintain its not for profit status members of its board must serve as volunteers, and inure no benefit from their work on the board. The executive director of the housing authority has the same requirements as all other members. All meetings for CHIG were conducted either before the normal work day began or after it was over, as all other members of the board had fulltime work obligations. All of the corporations which were set up by CHIG to develop and, in September of 2008 to operate the facility are also not for profit corporations of which the executive director is a board member have the same requirements. OMB circular A-87 does allow for donated services to be provided to a governmental agency.

6

Additionally, the policy of KCKHA is that employees have flex time at work and are expected to put in our normal work day (8 hours) any time between the hours of 7:00am and 5:30 pm. One of the purposes was to allow employees the opportunity to increase their community service commitments. So an employee that works from 7 to 5:30 and takes a thirty minute lunch could spend two hours each day on community service projects.

Finally, it is our belief that the development work at this agency has not impacted our public housing mission. Our PHAS and SEMAP scores have remained constant or risen. Our Monitoring reviews have continued to show improvement. Our occupancy has improved. Our financial condition has remained strong. For those reasons we do not believe that any of our development activities has impacted the services to our residents, the condition of our capital assets, or our financial ability to carry out our mission.

It is our understanding that we will be contacted after the audit report is provided to the local field office of public housing, and that we will then have the opportunity to resolve these outstanding findings.

OIG Evaluation of Auditee Comments

Comment 1 Notice PIH 2007-15 of June 2007, reiterated HUD restrictions on federal funding that already existed in annual contributions contracts between public housing authorities and HUD. The Authority entered into an annual contributions contract with HUD on January 23, 1996, well before OIG issued audit report 2004-AT-0001 in 2004. The contract stated the Authority may withdraw public housing funds only for the payment of development and operation costs of the projects under the contract or other purposes approved by HUD. Delaware Highlands Assisted Living did not contain public housing units, was not covered under the contract, nor was it approved by HUD.

Comment 2 We disagree that HUD changed its guidelines as a result of OIG audit report 2004-AT-0001. The OIG report pointed out to HUD an apparent misconception by public housing authorities regarding how such entities could use federal funds in development activities. HUD subsequently reminded public housing authorities of federal funding use restrictions that already existed in their annual contributions contract.

Comment 3 Our report did not detail the makeup of the $184,901 in federal funds inappropriately used for development activities. The $183,901 due from the nonprofit affiliate to the Authority was made up of $163,367 for Bethany Hospital development efforts and $20,534 for Delaware Highlands Assisted Living.

Comment 4 The Authority's annual plans described development activities in vague terms and stated that the Authority intended to pursue replacement of public housing units and development of assisted housing. The annual plans did not state that the Authority intended to use public housing funds for developments that did not contain public housing units.

Comment 5 The Authority accurately reported the amount due from its nonprofit affiliate in its annual audited financial statements. However, the Authority did not disclose in the notes to the financial statements that the amount due from the affiliate represented federal funds spent for nonfederal development activities.

Comment 6 We agree that the Authority was not without use of $1 million during the entire audited time period. However, nearly $1 million of the Authority's funds were not available for the intended purpose as of March 2005. The chart on page 7 of this audit report demonstrates the flow of federal funds to/from nonfederal development activities between January 2002 and December 2006.

Comment 7 The $1.5 million questioned represents payroll costs for employees that spent time working on federal and nonfederal activities during periods of the development efforts. These employees did not track the time they spent on federal or nonfederal activities. Therefore, we questioned their payroll costs for those periods in which they worked on both types of activities.