



Issue Date: September 30, 2002

Audit Case Number: 2002-SF-1006

TO: Charles H. Williams, Director HUD's Office of Multifamily Housing Assistance Restructuring, HY

//SIGNED//

FROM: Mimi Y. Lee, Regional Inspector General for Audit, 9AGA

SUBJECT: Audit Memorandum - Congressionally Requested Audit of the Outreach and Training Assistance Grant awarded to the Legal Aid Society of Hawaii, Honolulu, HI, Grant Number FFOT98006HI.

INTRODUCTION

We completed an audit of the Legal Aid Society of Hawaii's (LASH) Outreach and Training Assistance Grant (OTAG). The LASH performed OTAG activities and also distributed funds to the Affordable Housing and Homeless Alliance (AHHA) to perform OTAG activities on behalf of the LASH. The audit identified the grantee participated in questionable activity, and did not sufficiently confirm costs in compliance with the 1998 Notice of Funds Availability (NOFA), Office of Management and Budget's (OMB) Circulars, the applicable Codes of Federal Regulations (CFR), and the grant agreement. Our report contains four recommendations to address the issues identified in the report.

Section 1303 of the 2002 Defense Appropriation Act (Public Law 107-117) requires the HUD Office of Inspector General to audit all activities funded by Section 514 of the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA). The directive would include the Outreach and Training Assistance Grants (OTAG) and Intermediary Technical Assistance Grants (ITAG) administered by the Office of Multifamily Housing Assistance Restructuring (OMHAR). Consistent with the Congressional directive, we reviewed the eligibility of costs with particular emphasis on identifying ineligible lobbying activities.

In conducting the audit, we reviewed the grantee's accounting records and interviewed responsible staff. We also reviewed the requirements in MAHRA, the OTAG Notice of Fund Availability, the OTAG grant agreement, HUD's requirements for grant agreements for nonprofit entities, and OMB Circular A-122's guidance on the allowability of cost for nonprofit grantees.

The audit covered the period of October 1998 through June 2002 for the OTAG grant. We performed the fieldwork at the LASH office located in Honolulu, Hawaii, during July 2002. In addition, we obtained information from other OIG auditors, who performed a concurrent review at the AHHA office, located in Honolulu, Hawaii. We conducted the audit in accordance with Generally Accepted Government Auditing Standards.

We appreciate the courtesies and assistance extended by the personnel of the LASH during our review.

In accordance with HUD Handbook 2000.06 REV-3, within 60 days please provide us, for each recommendation without a management decision, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Additional status reports are required at 90 days and 120 days after report issuance for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the audit.

Should you or you staff have any questions please contact me at (415) 436-8101.

SUMMARY

The LASH submitted an application to HUD for OTAG funding and was awarded grant FFOT98006HI in February 1999. LASH planned to perform eligible tenant outreach, organizing, and training under the OTAG in coordination with the AHHA. Grant funds of \$22,157 were subsequently provided to the AHHA. Our audit identified the LASH charged the grant \$6,408 for tenant legal representation not allowed by the 1998 NOFA, OMB Circular A-122, or the grant agreement. In addition, the LASH did not sufficiently confirm \$10,904 in questionable sub grantee payroll expenses in accordance with the grant agreement; OMB Circular A-110; and 24 CFR Part 84, Uniform Administrative Requirements for Grants and Agreements with Nonprofit Organizations. Our report contains recommendations to address the issues identified in the report.

BACKGROUND

The Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA) established the Office of Multifamily Housing Assistance Restructuring (OMHAR) within HUD. Utilizing the authority and guidelines under MAHRA, OMHAR's responsibility included the administration of the Mark-to-Market Program, which included the awarding, and oversight of the Section 514 Outreach and Training Assistance and Intermediary Technical Assistance Grants. The objective of the Mark-to-Market Program was to reduce rents to market levels and restructure existing debt to levels supportable by these reduced rents for thousands of privately owned multifamily properties with federally insured mortgages and rent subsidies. OMHAR worked with property owners, Participating Administrative Entities, tenants, lenders, and others to further the objectives of MAHRA.

Congress recognized, in Section 514 of MAHRA, that tenants of the project, residents of the neighborhood, the local government, and other parties would be affected by the Mark-to-Market Program. Accordingly, Section 514 of MAHRA authorized the Secretary to provide up to \$10 million annually (\$40 million total) for resident participation, for the period 1998 through 2001. The Secretary authorized \$40 million and HUD staff awarded about \$26.6 million to 38 grantees (a total for 81 grants awarded). Section 514 of MAHRA required that the Secretary establish procedures to provide an opportunity for tenants of the project and other affected parties to participate effectively and on a timely basis in the restructuring process established by MAHRA. Section 514 required the procedures to take into account the need to provide tenants of the project and other affected parties timely notice of proposed restructuring actions and appropriate access to relevant information about restructuring activities. Eligible projects are generally defined as HUD insured or held multifamily projects receiving project based rental assistance. Congress specifically prohibited using Section 514 grant funds for lobbying members of Congress.

HUD issued a Notice of Fund Availability in fiscal year 1998 and a second notice in fiscal year 2000 to provide opportunities for nonprofit organizations to participate in the Section 514 programs. HUD provided two types of grants: (1) the Intermediary Technical Assistance Grant (ITAG), and (2) the Outreach and Training Assistance Grants (OTAG). The Notice of Fund Availability for the ITAG states that the program provides technical assistance grants through Intermediaries to sub-recipients consisting of: (1) resident groups or tenant affiliated community-based nonprofit organizations in properties that are eligible under the Mark-to-Market program to help tenants participate meaningfully in the Mark-to-Market process, and have input into and set priorities for project repairs; or (2) public entities to carry out Mark-to-Market related activities for Mark-to-Market-eligible projects throughout its jurisdiction. The OTAG Notices of Fund Availability state that the purpose of the OTAG program is to provide technical assistance to tenants of eligible Mark-to-Market properties so that the tenants can (1) participate meaningfully in the Mark-to-Market program, and (2) affect decisions about the future of their housing.

OMHAR also issued a December 3, 1999 memorandum authorizing the use of OTAG and ITAG funds to assist at-risk projects. OMHAR identified these as non-Mark-to-Market projects where the owners were opting out of the HUD assistance or prepaying the mortgages.

HUD's regulations at 24 CFR Part 84 contain the uniform administrative requirements for grants between HUD and nonprofit organizations. The regulations (24 CFR 84.27) require that nonprofit grantees utilize OMB Circular A-122, Cost Principles for Non-Profit Organization, in determining the allowability of costs incurred to the grant. OMB Circular A-122 outlines specific guidelines for allowability of charging salaries and related benefits to the grants and the records needed to support those salaries. For indirect costs charged to the grant, the Circular establishes restrictions for indirect costs, and specific methods and record keeping to support the allocation of costs.

The Circular also establishes the unallowability of costs associated with Federal and state lobbying activities. Simply stated, the use of federal funds for any lobbying activity is unallowable. OMB Circular A-122 identifies some examples of unallowable lobbying activities.

These include any attempt to influence an elected official or any Government official or employee (Direct Lobbying) or any attempt to influence the enactment or modification of any actual or pending legislation by propaganda, demonstrations, fundraising drives, letter writing, or urging members of the general public either for or against the legislation (Grassroots Lobbying).

LASH is a corporation organized under the laws of the State of Hawaii. On January 25, 1972, the IRS determined that LASH was exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code. The objective and purpose of LASH is to equip, maintain, and operate offices and to employ attorneys to render legal assistance to worthy persons who are in need of such help but who are unable to pay for it, and by reason thereof might be denied equal protection under the laws; to solicit, receive, and provide funds to engage in such activities as are usual and legal and proper for legal aid societies; and to secure justice for and to protect the rights of the needy and to promote measures for their assistance in such connection. The mission of LASH is to achieve fairness and justice for Hawaii's people through quality representation, advocacy, community partnerships, education, and outreach. Under the Community Education Outreach program, LASH provides outreach and training to Section 8 tenants who live in buildings with expiring Section 8 subsidies by informing them of the process and assisting tenant associations. There are over 40 other programs that LASH is involved in that are funded through various Federal and non-Federal sources. For fiscal years ending June 30, 2000 and 2001, this included other HUD funding of \$121,020, and Maui Community Development Block Grant funds of \$37,500.

LASH applied for OTAG funding on June 26, 1998. HUD awarded \$50,000 to the LASH under grant agreement FFOT98006HI in February 1999. LASH began drawing down funds from the grant starting in June 1999, which included expenses back to October 1998. As of July 2002, the LASH had drawn down \$48,090 of the grant funds. Between 1999 and 2000, LASH provided \$22,157 of grant funds to the AHHA, which had not yet applied for its own OTAG grant. The AHHA subsequently applied for and received its own OTAG funding [Note: OTAG funds awarded directly to the AHHA were reviewed under a separate concurrent audit, the results of which will be reported under a separate cover]. The LASH received annual financial audits of their activities for the years ending June 30, 1999, 2000, and 2001. The auditor provided an unqualified opinion for each of the three years.

FINDING
The Grantees Did Not Comply With HUD and OMB Requirements

The LASH charged the grant \$6,408 for questionable legal representation activities. In addition, the LASH did not adequately confirm \$10,904 of questionable sub grantee payroll. As a result, less funding was available for eligible tenant outreach, organizing, and training under the Mark-to-Market program. This occurred because LASH placed a low priority over the confirmation of sub grantee activity, and LASH was not sufficiently familiar with program requirements.

Questionable Legal Representation

The 1998 NOFA defined the purpose of the OTAG program as to provide funds to conduct outreach and training development for HUD tenants in properties eligible to participate in the Mark-to-Market (M2M) program, so the tenants can participate in the M2M program and affect decisions about the future of their housing. Eligible activities include:

1. Identifying residents and resident groups living in eligible properties;
2. Providing outreach and training to tenants to explain the M2M program, the possible financial changes, the possible project repairs, access and community resources and effective methods for communicating the organization's position;
3. Organizing residents of eligible low-income housing so the tenants can effectively participate in the M2M process;
4. Performing outreach, training, and counseling, which may include teaching sound housing management, maintenance, and financial management, to residents and resident groups living in eligible M2M properties;
5. Delivering training programs on M2M and/or resident homeownership options;
6. Establishing M2M clearinghouses as a resource to resident organizations, community groups and potential purchasers;
7. Creating informational materials about the M2M process for distribution;
8. Providing support for HUD approved activities proposed by the grantee that would further the M2M program and others considered eligible at HUD's discretion; and
9. Educating parties outside HUD about the M2M process.

The OTAG grant agreement FFOT98006HI between HUD and LASH incorporated the grant application, which described LASH's planned activities under the OTAG grant. Activities described included outreach, organizing, and training efforts similar to eligible activities identified in the NOFA. Neither the application nor the agreement proposed using OTAG funds to provide legal representation concerning tenancy issues.

Federal regulations at 24 CFR 84.25, Revisions of budget and program plans, requires recipients to report deviations from budget and program plans, and request prior approvals for budget and program plan revisions, including changes in the scope or the objective of the project or program and changes in a key person specified in the application or award document.

OMB Circular A-122, Attachment A, states that for costs to be allowable, the costs must be reasonable, ordinary and necessary for the performance of the award, and allocable to the grant in accordance with the benefits received.

HUD issued a letter on December 3, 1999 expanding the types of projects eligible for OTAG assistance. However, it does not allow OTAG funds to be used to represent tenants in legal matters relating to civil rights complaints, inappropriate charges, and harassment by owners.

In 2001, the LASH began charging staff time to represent tenants in their pursuit of legal and management issues relating to their tenancy. The progress reports submitted to OMHAR showed these cases related to retribution by management when tenants began organizing under the OTAG program. The LASH pursued the following cases on behalf of the tenants:

- Case 00-10-03009607 involved tenant(s) of the Kulana Nani housing development being harassed by the manager,
- Case 00-10-02007350 involved a tenant's uncorrected maintenance problems at the Kulana Nani housing development. Respondents to the matter were the City and County of Honolulu, the management agent, and HUD,
- Case 01-10-02002301 involved a tenant's challenge of the management's Section 8 and Section 236 rent calculations, and
- Case 01-10-02002589 involved a tenant's eviction from the Kulana Nani housing development for nonpayment of rent.

LASH charged its attorney's payroll costs associated with time spent on these cases. Overall, this included 267 hours at \$20 per hour, with 20 percent fringe benefits, which totaled \$6,408. The following table summarizes the hours spent on the cases and attributed to the OTAG program:

Month	00-10-03009607	00-10-02007350	01-10-02002301	01-10-02002589	Total
Jan-01	47				47
Feb-01	15.5	1.5			17
Mar-01	2	2	1.5		5.5
Apr-01	46	12	4.25	8.5	70.75
May-01	11.25	10.5	5.5	1.5	28.75
Jun-01	10		3	6.75	19.75
Jul-01	63	0.75			63.75
Aug-01	4				4
Sep-01	6.5	4			10.5
Total:	205.25	30.75	14.25	16.75	267

LASH interpreted HUD's December 3, 1999 letter as allowing OTAG funds to be used for other purposes related to HUD projects. LASH claimed it consulted with an OMHAR representative concerning its conclusion that working with the tenants included representing them in their effort to settle tenancy issues with the property management or, failing that, represent the tenants in the court of law. However, LASH could not produce documented approval from HUD, showing the activity was eligible. Nothing in the grant agreement, NOFA, CFR or OMB criteria state this activity was an appropriate under the OTAG program. As a result, there was less funding available for eligible tenant outreach, organizing, and training for tenant groups under the Mark-to-Market program.

Inadequate Monitoring of AHHA Results in Questionable Payroll Expenses

As part of the OTAG agreement, FFOT98006HI, LASH agreed to accept responsibility for compliance by any other entities to which it makes grant funds available, with the NOFA and any other applicable laws, regulations and requirements (including record keeping requirements), and with the activities listed in the grantee's application.

OMB Circular A-110, Section 51, states recipients are responsible for managing and monitoring each program, activity, and sub award.

Federal regulations at 24 CFR 84.21 requires grantees to maintain records adequately identifying the source and application of funds, and maintain accounting records that are supported by source documentation. Section 84.85, Reports and records, makes grantees responsible for managing and monitoring each project, program, subaward, function or activity supported by the award. In addition, financial records, supporting documents, statistical records, and all other records pertinent to an award shall be retained for a period of three years from the date of submission of the final expenditure report.

OMB Circular A-122, Attachment A, prescribes cost allocation methods including direct and indirect. Allowable indirect cost allocation methods include the simplified allocation method and the multiple allocation base method. Attachment B, Paragraph 7, Compensation for Personal Services, states that reasonable compensation and fringe benefits to employees are grant fundable costs. The Circular also places specific salary record keeping requirements on the grantee. The grantee must maintain reports that account for the total activity an employee is compensated for in fulfillment of their obligations to the organization. The reports must reflect an after the fact determination of actual activity for each employee. Budget estimates do not qualify as support for charges to the grant. Grantees must also maintain reports reflecting the distribution of activity of each employee (professionals and nonprofessionals) whose compensation is charged, in whole or in part, directly to awards. In addition, in order to support the allocation of indirect costs, such reports must also be maintained for other employees whose work involves two or more functions or activities if a distribution of their compensation between such functions or activities is needed in the determination of the organization's indirect cost rate.

The LASH did not inspect AHHA records to confirm disbursements, which resulted in questionable payroll costs of \$10,904. LASH provided grant funding to the AHHA between October 1998 and December 2000 to perform OTAG related activity. The LASH only required

the AHHA to submit time sheets, which was inadequate to ensure payroll costs were appropriate. This occurred because the LASH did not place sufficient priority over substantiating costs, and lacked established procedures for reviewing sub grantee costs.

The total amount charged to the grant for AHHA activities during this period was \$22,157. This amount was for payroll expenses, of which \$18,464 was for salary and \$3,693 was for the benefits of the Executive Director. Although the AHHA did submit reports to the LASH showing 900.25 hours worked on the OTAG program, there is no information to show the LASH confirmed the AHHA's actual payroll costs.

The LASH established an hourly salary rate of \$20.51 and a benefits allocation of 20 percent for the AHHA's Executive Director. However, the LASH did not substantiate the AHHA incurred these costs. There was also inadequate payroll and accounting documentation available at the AHHA in July 2002 to establish whether the Executive Director was actually paid the rate charged, or establish whether the benefits costs were reasonable.

However, based on discussions with the AHHA Executive Director, the AHHA Board approved full-time annual salary of the Executive Director was \$24,000 between 1998 and 2000. As a result, the appropriate hourly salary rate should have been \$12.50, and the total salary reimbursement should have been \$11,253. The questionable difference of \$7,211 represents OTAG funds that could have been used to fund other OTAG related tenant outreach and training.

AUDITEE COMMENTS AND OIG EVALUATION OF AUDITEE COMMENTS

We provided our draft report to the grantee for its comments on August 30, 2002. The grantee provided their comments on September 16, 2002. We included the LASH's comments in Appendix B of the report. We also obtained further clarification during an exit conference discussion with a LASH official on September 25, 2002.

The LASH disagreed with our conclusions. Its interpretation of the December 3, 1999 letter from OMHAR allowed for the use of OTAG funds for legal services. The legal representation in question related to management retribution against tenants in their attempt to organize under the OTAG program. LASH also stated these activities were fully identified on progress reports submitted to OMHAR. Since OMHAR approved the associated withdrawal of grant funds, it also effectively approved the activity.

We acknowledge the legal representations related to management retribution against tenants' efforts to organize, and this information was disclosed on the progress reports submitted to HUD. We have adjusted the report to reflect this information. However, no criteria state such legal representations were appropriate under the OTAG program. The activity was not included in the LASH's grant agreement, and no specific HUD approval was available. However, based on LASH's response, we adjusted the issue from an ineligible cost to an unsupported/questioned cost. We conclude there is a need for HUD to make a determination on the eligibility of the activity.

The LASH also disagreed with our conclusions over the AHHA's payroll costs, including salary and benefits. The LASH listed the AHHA Executive Director's annual salary as \$36,000. The \$24,000 figure represented the Executive Director working only two-thirds of full time. In addition, 10 percent was added to the pay rate to compensate for other unidentified costs. The LASH also listed its determination of what the AHHA's Executive Director should have been paid for benefits. The LASH stated it had an understanding with the AHHA that the amounts would be paid, and the LASH should therefore not be held liable for what the AHHA did.

The OTAG grant was awarded to the LASH, and the LASH chose to provide funds to the AHHA. The OTAG grant agreement, OMB, and CFR criteria require the grantee to ensure the costs of sub grantees are appropriate. The LASH did not take adequate steps to ensure the accuracy of the sub grantee's costs, or ensure the sub grantee properly accounted for and documented these costs. The auditee has provided no information to demonstrate the amounts disbursed to the AHHA were appropriate. In addition, no support has been provided to demonstrate the 10 percent allocation of other costs was appropriate within the guidelines of OMB Circular A-122. However, based on the LASH's response, we have adjusted the questioned salary costs from ineligible to unsupported.

RECOMMENDATIONS

We recommended you:

- 1A. Obtain a legal determination as to whether the use of OTAG funding for tenant legal representation is appropriate under the OTAG program. If not, require the LASH to return the \$6,408 of OTAG funds used for legal representation.
- 1B. Require the LASH to submit documentation to confirm the benefits allocation was appropriate based on the AHHA's actual benefits costs, or return the unsupported \$3,693.
- 1C. Require the LASH to submit payroll documentation to support salary costs paid to the AHHA, or return the \$7,211 of questioned salary costs.
- 1D. Consider suspending grant funding until the grantee develops and implements appropriate management controls to ensure only eligible activities receive funding and the documentation for the expenditure complies with OMB Circular A-122.

MANAGEMENT CONTROLS

In planning and performing our audit, we considered the management controls relevant to the LASH' Section 514 program to determine our audit procedures, not to provide assurance on the controls. Management controls include the plan of organization, methods, and procedures adopted by management to ensure that its goals are met. Management controls include the processes for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

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

- Controls and procedures over grant activities and related disbursements,
- Controls and procedures over monitoring activities and costs of sub recipients,
- Controls and procedures over grant receipts, and
- Controls and procedures over the reporting of activities and cost.

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

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

- Lack of a procedures to ensure grant activities were eligible under program requirements, and
- Lack of polices and procedures over monitoring activities and costs of sub recipients.

FOLLOW-UP ON PRIOR AUDITS

The Office of Inspector General performed no previous audit of the LASH.

SCHEDULE OF QUESTIONED COSTS

Recommendation Number	Type of Questioned Costs	
	Ineligible 1/	Unsupported/Questioned 2/
1A		\$6,408
1B		\$3,693
1C		\$7,211

- 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/Questioned costs are costs charged to a HUD-financed or HUD-insured program or activity and eligibility cannot be determined at the time of audit. The costs are not supported by adequate documentation or there is a need for a legal or administrative determination on the eligibility of the costs. Unsupported costs require a future 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.

AUDITEE COMMENTS

Legal Aid Society



- of Hawaii -

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September 16, 2002

Ms. Mimi Y. Lee
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General
Pacific/Hawaii District
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San Francisco, CA 94102-3448

Dear Ms. Lee:

In response to your letter dated August 30, 2002 we have reviewed our systems and procedures regarding the Outreach and Training Assistance Grant (OTAG) numbered FFOT98006HI and have found the following with regard the recommendations made by the HUD Auditor:

Recommendation 1A.

- Require the LASH to return the \$6,408 of OTAG funds used for other legal representation.

The Draft Finding incorrectly describes the information which LASH provided to the Auditor, and incorrectly states that "LASH could not produce documented authority from HUD" authorizing LASH's use of OTAG funds in accordance the December 3, 1999 letter authored by Ira G. Peppercorn, Director of HUD OHMAR ("Peppercorn Memo"). See Draft Finding, p. 2. Relying upon these two statements of misinformation, the Draft Finding recommends that LASH return to HUD \$6,400.00 of OTAG funds.

The Draft Finding's recommendation is in error and unsupportable because: (1) LASH submitted with its quarterly report dated July 5, 2001 a complete explanation of the OTAG activities for which it was seeking reimbursement; (2) LASH attached the Peppercorn Memo to its July 5, 2002 report, with the explanation that, per LASH's understanding, the Peppercorn

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Memo set forth the language which authorized OTAG funding for the activities described in the report; and (3) HUD, with the benefit of all information provided by LASH's good faith and full disclosure, made the reasonable and supportable determination that the activities LASH had undertaken were a permitted use of OTAG funds, and reimbursed LASH for its reported activities. The Draft Audit and the Auditor's activities discovered no new information that had not been provided to HUD in July 2001. However, the Draft Audit attempts to disavow the decision that its agency had made with full knowledge in July 2001, and force LASH to disgorge the \$6,400.00 which HUD paid to it over a year ago. The Draft Audit's conclusion and recommendation are not supportable.

1. CORRECT RECITATION OF FACTS

Because the Draft Audit incorrectly describes the facts which were relayed to the Auditor regarding both the nature of certain activities engaged in by LASH, and how LASH received HUD's authorization to engage in certain advocacy and litigation activities, we set forth below an accurate and complete description of facts. These are the facts as they were presented not only to the Auditor during his recent visit, but to HUD in 2001, as verified by the LASH OTAG quarterly reports previously submitted to HUD.

LASH began conducting OTAG activities sometime in about February 1999. It performed under its grant in cooperation with the Affordable Housing and Homeless Alliance ("AHHA"). AHHA is a not-for-profit organization of tenant organizers. Generally, LASH legal counsel and AHHA organizers would work cooperatively on OTAG activities, combining their efforts to offer organizing techniques and legal and technical advice to tenants at eligible properties.

On December 3, 2002, the Peppercorn Memo was issued to LASH. The Peppercorn Memo expanded the permissible use of OTAG funds. It provided:

In order to ensure tenants have a voice, ITAGs and OTAGs also will be allowed to work with residents of above market properties, where contracts are close to expiration, where owners are opting out of the program or prepaying their mortgage, where substandard conditions or poor management exists, where ownership transfers that preserve the building as affordable housing are underway, or where an owner has been deemed ineligible for M2M.

Peppercorn Memo, p. 1-2 (emphasis added).

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A. Kulana Nani: Pale and Ludloff

Beginning in October of 2000, tenants at Kulana Nani, an OTAG eligible property owned by the City and County of Honolulu, began complaining to AHHA and LASH OTAG staff about serious management problems and substandard conditions at their property. Tenants had been attempting to organize a tenant association with the organizing assistance of AHHA staff to address existing problems with building maintenance and management practices. However, rather than supporting the organizing effort as is its legal duty, the resident management staff began to issue house rules violations against tenants for participating in organizing activities. Appeals were made by tenants to the management company, the City staff who oversaw building management, and even the press. The management's retaliatory acts only grew worse. AHHA staff and LASH staff stepped up from their normal roles supporting and advising the tenants, and appealed to the management company and the City directly. They received no response, and the retaliatory acts grew even worse. The situation was truly desperate. The tenants had serious issues relating to their rights as tenants and quality of housing which they wanted discussed, but every time they attempted to raise an issue, they came one step closer to being evicted by a hostile resident manager, and apathetic owners who took no remedial steps.

The tenants and AHHA and LASH staff made every effort to resolve this issue through supporting and advice. Unfortunately, it became necessary to file suit to protect the tenants' rights to organize and the OTAG grantees rights to help the tenants organize. As described in LASH's July 5, 2001 OTAG report (as well as in its April 2, 2001 report), LASH OTAG staff prepared a complaint which was filed in federal district court. No trial was ever held, but the suit forced the management company and the City to respond, and ultimately, enter into a settlement agreement under which it agreed to take several measures protective of organizing activities at not only Kulana Nani, but at the City's other Section 8 building, Westlake Apartments.

In about June 2001, LASH OTAG staff contacted its existing contact, Dennis O. Dorsey, to clarify that the advocacy and litigation undertaken by LASH at Kulana Nani were permitted OTAG activities per the Peppercorn Memo. Contrary to the statement made in the Draft Audit, LASH does not claim to have received authorization from Mr. Dorsey to consider these activities as OTAG activities. What Mr. Dorsey said – and what LASH relayed to the Auditor – was that he was not familiar with the Peppercorn Memo, but that LASH should attach it to its next report so HUD could determine if it permitted the reported activities under OTAG. As evidence by the July 5, 2001 quarterly report, LASH did just that. LASH explained in detail the activities undertaken by it at Kulana Nani, the purpose for the activities, the results of the activities, and the explanation that “the OTAG policy relied upon by LASH staff in pursuing these OTAG activities is attached hereto as Exhibit ‘B.’” See July 5, 2001 Quarterly Report Narrative.

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The Peppercorn Memo was attached as Exhibit "B." To ensure that HUD would note the nature of the reported activities, and would have full information on the details of the events which necessitated the advocacy and litigation activities, LASH also attached a copy of the 21 page federal court complaint, and its 19 page exhibit, to the July 5, 2001 report, as Exhibit "A."

There can be no argument over whether LASH completely disclosed to HUD the activities it had engaged in and its explanation of why it considered such activities to be OTAG activities. With all of this information before it, HUD recognized the advocacy and litigation activities as permitted under the OTAG grant, and HUD expressed this recognition by subsequently issuing funds to LASH in reimbursement for undertaking these activities.

The Auditor's investigation did not discover any information that HUD did not have when it issued the OTAG funding in response to the July 5, 2001 report. If HUD at this time determines that as a matter of policy that it does not wish to consider such activities to be funded by OTAG, it is free to do so with prospective effect. However, HUD has no ground to request that a grantee disgorge funds which it received over a year ago, when that grantee was acting reasonably, in good faith and with complete honesty and disclosure.

As evidence of LASH's good faith and openness in dealing with HUD as an OTAG grantee, we invite you to compare LASH's quarterly reports to those of other grantees. Because the HUD reporting form does not provide adequate space for full and accurate disclosure of activities, LASH has always supplemented the form report with a detailed narrative of its activities. While LASH has no access to the reports of other grantees, it was informed by OHMAR staff in about May 2001 that its quarterly reports were the most informative. On this complement, LASH was not only made proud of its activities, but was ensured that HUD staff actually read the reports. Thus, when it submitted its July 5, 2001 report, with its explanation of activities and supporting documents, it was assured that HUD staff would review its report and make a determination regarding the Kulana Nani activities and the Peppercorn memo. Presumably, that determination was made, and HUD reimbursed LASH for its activities.

B. Kulana Nani: Kelly and Makaila

When the new management company began at Kulana Nani in April 2001, it encountered serious difficulty in calculating certain tenants's rents and rent balances because the prior management company had kept very poor records and miscalculated rents. Ms. Kelly and Mr. Makaila were among the tenants who were being harmed by this mismanagement and the difficulty the new management company was having in sorting it out. As a matter of policy, the new management company was going strictly by what it had in the remaining files. Often times, however, tenants such as Ms. Kelly and Mr. Makaila had documentary evidence that what was in

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their files was not accurate. LASH staff was invited by both the tenants and the new management company to help facilitate solutions to these conflicts, and to help the management company set fair and reasonable policies for addressing these situations.

The Draft Finding is simply incorrect in its description of the Makaila case as involving an eviction. Although there may have been an eviction action filed at one time, prior to LASH's involvement, based upon the rent calculation errors, LASH's involvement was not concerned with the eviction action. LASH staff was involved only in facilitating solutions among the management and tenants that were a result of the error-riddled files, and in improving the management company's practice with regard to addressing these conflicts. LASH staff never made any court appearances or participated in any litigation regarding Mr. Makaila, or Ms. Kelly, for that matter.

Again, as with the Pale and Ludloff activities, LASH staff fully disclosed to HUD the activities it undertook with regard to Mr. Makaila and Ms. Kelly, and HUD, upon that information, issued funds to LASH in compensation. Also like the Pale and Ludloff activities, the involvement of LASH staff addressed and remedied poor management practices, as described in the Peppercorn Memo.

II. ANY ATTEMPT BY HUD TO RECLAIM FUNDS IS ILLEGITIMATE AND NOT SUPPORTABLE AT LAW

As described above, LASH's actions under the OTAG grant have all been taken in good faith and reasonable reliance upon the Peppercorn Memo and subsequent HUD action.

The Peppercorn Memo expanded original OTAG-permitted activities "to ensure tenants have a voice . . ." See Peppercorn Memo, p. 1. LASH successfully effected this purpose through its range of activities at Kulana Nani, which began with organizing and technical assistance, but developed into a more consuming effort due to the management and owner's aggressive resistance to tenant organizing and other management problems. Although consuming, the efforts at Kulana Nani succeeded in improving management of Kulana Nani immeasurably. It also improved management of the City of Honolulu's other Section 8 property. Ultimately, the Kulana Nani OTAG activities tangibly improved the living conditions of hundreds of low-income families in Honolulu County.

When the standard organizing and assistance techniques did not succeed at Kulana Nani for identifiable reasons, LASH stuck with the tenants at Kulana Nani to see that the end goal of OTAG funding was met: to ensure that tenants had a voice and the ability to address serious management problems. LASH explained completely and in detail to HUD what activities it

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engaged in at Kulana Nani to ensure that this goal was met. HUD received this information, processed it, and awarded LASH OTAG funding in reimbursement for these activities. By doing this, HUD expressed its consent to such activities being undertaken under OTAG. Based upon this consent, LASH continued its work at Kulana Nanni and undertook other work that ultimately improved the management of the long-neglected property.

As HUD is aware, LASH is a not-for-profit legal services organization with a limited budget. Forcing LASH to disgorge funds which it earned honestly and in good faith would cause significant and unjustifiable harm to LASH.

For the reasons described above, it should be clear that it would be greatly unfair to force LASH to disgorge any OTAG funds. However, being unfair, HUD has no right to demand that LASH disgorge any OTAG funds as a simple matter of contract law. Putting aside other obvious issues of estoppel and reliance, LASH provided a service which was reasonable to deliver under its contract, HUD had full knowledge of the service provided, expressed its consent and satisfaction as to the service, and paid LASH for the service. A year later, HUD, with no new information of any kind, has apparently decided that it does not approve of the service after all. This after-the-fact second thought by HUD is an internal problem for HUD to deal with on an internal level. It gives HUD no right to demand a return or any funds from LASH.

Recommendation 1B.

Require the LASH to submit documentation to confirm the benefits allocation was appropriate based on the AHHA's actual benefits costs, or return the unsupported \$3,693.

LASH calculation of Ms. Hasegawa's benefits (based on 20%) were as follows:

FICA	7.65	$206/m \times 12 = 2472/yr$
Unemployment Insurance	3.50	$2472/24000 = 10.3$
Worker's Comp. Ins.	.54	
Temp. Disability Ins.	.46	
Medical Insurance	<u>10.30</u>	
	22.45	

Employers are required to pay FICA by Federal Mandate. The last four line items are State mandated requirements for employers to provide employees in the State of Hawaii. In good faith, LASH paid these amounts to AHHA with the understanding that designated "fees" for the line items above would be paid. Therefore we feel that LASH is not and should not be held

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responsible for any penalties, interests or fines as a result of any noncompliance to governmental regulations by AHHA or any other representative party.

Recommendation 1C.

Require the LASH to return the \$7,211 of unreasonable salary costs paid to the AHHA.

With regard to LASH oversight of AHHA activities, the audit report incorrectly states that "LASH only required a verbal activity report from AHHA, and did not require documentation of activities to be submitted." To the contrary, throughout the grant period, LASH staff traveled to the AHHA office twice per month to review project work, collect documentation of activities, and collaboratively determine which HUD assisted projects should be engaged for outreach and training, based on grant criteria. At these meetings, AHHA provided written documentation in the form of flyers for meetings, project contact summaries and issue reviews for the developments where AHHA was conducting outreach. AHHA staff obtained documents from project owners and PAEs related to the Mark to Market (M2M) process which were provided to LASH. In addition, LASH attended meetings held at the HUD assisted developments which were organized by AHHA staff, and LASH also observed AHHA staff at M2M tenant consultation meetings. Further evidence of sub-grantee's activity is reflected in LASH records documenting responses to tenant questions generated as a result of AHHA outreach activity. Moreover, the only costs LASH paid were staff time for supervision of these outreach activities. Given the fact that LASH staff personally observed AHHA's successful efforts to engage and educate tenants about HUD programs, and the M2M process in particular, at each and every building referred for M2M review in the state of Hawaii through the grant period, the draft Inspector General's audit has no basis to conclude that LASH lacked assurance that reported activities actually occurred.

LASH paid AHHA salary costs based on a salary of \$24,000 for 2/3 time position. Based on 1,950 hours per year, 2/3 of that time or .66 is 1,287 hours. Craig Castellanet acted as LASH's representative to AHHA's Board. As a board member Mr. Castellanet confirms the aforementioned amount for the time period noted above as Ms. Hasegawa's salary. It is important to note that Ms. Hasegawa's present salary is \$36,000 per year.

$$\begin{aligned} \$24,000/1,287 &= \$18.64 \text{ per hour} \\ \$18.64 \times 1.1 &= \$20.51 \end{aligned}$$

The 10% is for other expenses such as supplies, mileage which were not to be billed separately. AHHA Executive Director would actually work longer hours on a voluntary basis. Ms.

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Hasegawa's salary did not change during the period in question.

CONCLUSION

We hope that HUD understands from the above description, a review of the quarterly reports submitted by LASH, and a review of its own actions in this case, that it cannot and should not make any claim for the return of any funds from LASH. If you have any questions in this regard, please do not hesitate to contact myself, Wayne Keawe at (808) 536-4302.

Respectfully submitted,



Wayne Keawe
Comptroller

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