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TO: William F. Bolton, Director, Los Angeles Multifamily Housing, 9DHMLA

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

SUBJECT: The Owner and Agent of Holiday Apartments, LA Pro 30, and Two Worlds II, Los Angeles, California, Mismanaged Project Finances and Operations

HIGHLIGHTS

What We Audited and Why

We audited the four Holiday Apartments (101-A, 101-B, 101-C, and 102), LA Pro 30, and Two Worlds II, housing projects which have U.S. Department of Housing and Urban Development (HUD)-insured financing and receive project-based Section 8 subsidy assistance. We initiated the audit in response to a request from HUD's Departmental Enforcement Center. Our objectives were to assess HUD's concerns over inappropriate disbursements and determine whether the projects were administered in compliance with HUD requirements.

What We Found

The owner and identity-of-interest management agent for the six projects used project funds to pay \$2,670,118 in ineligible and unsupported costs, including \$1,562,193 for excessive and unreasonable charges by an identity-of-interest maintenance contractor, \$365,734 in excessive charges for accounting services paid to identity-of-interest contractors, \$380,670 in payroll charges for the management agent's president, \$209,441 in unsupported rent charges and \$140,880 in capital improvement expenses for the management agent's office, and \$11,200 in ineligible ownership expenses. We anticipate similar additional

questionable costs continued after the end of our audit period, through June 2006, that could cost the projects another \$457,444.

In addition, the owner did not maintain the projects in good repair and free of health and safety violations. Our unit and building inspections identified more than 240 housing violations, which resulted in \$561,600 in housing assistance payments for units and buildings that were not decent, safe, and sanitary.

Finally, the owner and identity-of-interest management agent did not effectively manage the projects. They failed to ensure that project costs were reasonable and necessary; did not ensure that the properties were adequately maintained; and did not accurately calculate, report, and resolve \$655,173 in project liabilities.

What We Recommend

We recommend that the director of HUD's Los Angeles Multifamily HUB require the owner to repay the respective projects \$2,319,797 for the ineligible costs identified during our audit and review costs incurred after our audit period. HUD should require the owner to provide support over the reasonableness of the \$350,321 in unsupported costs or require the owner to repay the projects. We also recommend that HUD require the owner to correct unit deficiencies and certify they have been completed. In addition, HUD should require the owner to obtain new management, accounting, and maintenance services from entities that have no identity-of-interest with the owner; properly address project liabilities; and develop written procedures and controls over the projects' operations.

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

Auditee's Response

We provided our discussion draft audit report to the owner's general partner on January 20, 2006, and held an exit conference on February 8, 2006. The owner's general partner provided written comments on February 21, 2006, with additional comments on February 23, 2006. The ownership generally disagreed with our report findings.

The complete text of the auditee's response without the voluminous exhibits, along with our evaluation of that response, can be found in appendix B of this report. The exhibits will be made available upon request.

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BACKGROUND AND OBJECTIVES

Holiday Apartments consists of four U.S. Department of Housing and Urban Development (HUD)-insured housing projects (101-A, 101-B, 101-C, and 102), each under a separate regulatory agreement. Each project is owned by a limited liability partnership, whose general partner is also the general partner of two additional HUD-insured projects, LA Pro 30 and Two Worlds II. HUD insured all six projects under the Section 236 program between 1971 and 1974. The intent of the Section 236 program is to reduce rental costs for lower income families by subsidizing the property owners' mortgage interest payments.

In addition to interest subsidies, these scattered-site properties receive project-based Section 8 subsidies for their rental units. Under this program, HUD subsidizes tenant rent by paying the portion of the rent that exceeds 30 percent of eligible tenants' adjusted income. Collectively, the projects have 609 of their 632 units under the Section 8 program.

No.	Project name	Project Federal Housing Administration number	Mortgage amount	Regulatory Agreement date	Housing Assistance Payment contract (Section 8)
1	Holiday 101-A	122-44538-LDP-EC	\$ 1,490,500	November 1, 1971	CA16M000223 & CA16L000024
2	Holiday 101-B	122-44539-LDP-EC	\$ 1,525,500	November 1, 1971	CA16L000025
3	Holiday 101-C	122-44540-LDP-EC	\$ 1,536,200	November 1, 1971	CA16M000225 & CA16L000078
4	Holiday 102	122-44553-LDP-EC	\$ 1,148,300	August 31, 1972	CA16M000087 & CA16M000231
5	LA Pro 30	122-44542-LDP-EC-SR-PR	\$ 1,841,100	June 28, 1974	CA16L000075
6	Two Worlds II	122-44730-LDP-EC	\$ 1,150,200	December 5, 1973	CA16L000044

Proland Management Company, LLC, has acted as the management agent of the projects since October 1998. The projects' general partner is a co-owner of the management agent, and his principal place of business is located in the same building in which the management agent operates. Proland Management Company receives management fees, as set out in its management certifications, for managing the projects. These fees range from 12.18 to 15.01 percent of income collected, depending on the project. Between 2000 and 2004, the management agent charged the six projects more than \$2.2 million in management fees. The management agent also managed at least three additional non-HUD-insured projects owned by the general partner. In addition, the general partner and management agent engaged other identity-of-interest companies (in which the general partner had an ownership interest) to provide maintenance and accounting services, including Action Maintenance, Action Bookkeeping, and Accounting Data Systems.

The regulatory agreements restrict the amount of distributions an owner can take from the limited dividend projects to the prior year's surplus cash calculation, as reported on the projects' annual audited financial statements. Holiday 101-A and Two Worlds II had negative surplus cash during the entire audit period. The other four projects had intermittent surplus and negative surplus cash between 2000 and 2004, and only Holiday 102 had surplus cash for 2004. Further, distributions of surplus cash cannot be made if a project's physical condition does not meet HUD-established housing standards. HUD's Real Estate Assessment Center performs

inspections on the properties to assess their physical condition. The latest inspections showed Holiday 101-A and Holiday 101-B did not meet an acceptable level of housing standards in March 2005 and September 2005, respectively. Two Worlds II, Holiday 101-C, Holiday 102, and LA Pro 30 did meet acceptable housing standard levels during their respective September 2002, May 2003, July 2003, and February 2005 inspections. Holiday 102 and 101-A also did not meet an acceptable level on a prior 2000 and 2001 inspection, respectively.

The 2000 audited financial statements for the projects questioned project funds used to pay for payroll costs of supervisory staff, capital improvements to the agent's offices, and high maintenance costs. The following year, the owner contracted with a different independent public accounting firm to prepare the audited financial statements. The previous year's audit issues were cleared by the new accounting firm without explanation.

HUD's Departmental Enforcement Center referred the four Holiday Apartment projects to the Office of Inspector General (OIG) in October 2004, expressing concerns over the possible misuse of project funds. Accordingly, our objectives were to determine whether HUD's concerns had merit, to assess whether the projects were being administered in compliance with the regulatory agreement and other HUD requirements, and to ensure the projects met proper health and safety requirements. Due to the common ownership and management, we expanded our review to include both LA Pro 30 and Two Worlds II.

RESULTS OF AUDIT

Finding 1: The Projects Paid \$2,670,118 for Ineligible and Unsupported Expenses

The projects' general partner (owner) and identity-of-interest management agent used \$2,670,118 in project funds for ineligible and unsupported expenses. The owner/management agent used identity-of-interest contractors to charge the projects \$1,562,193 for excessive and unreasonable maintenance costs and \$365,734 for excessive accounting costs. Additional questionable costs paid included \$380,670 in ineligible payroll charges for the management agent's president, unsupported rent charges \$209,441 and capital improvement expenses \$140,880 for the management agent's central office, and \$11,200 in ineligible ownership expenses. We also estimate the projects were or will be charged another \$457,444 for questionable maintenance, accounting, and central office rent from the end of our audit period through June 2006. Payment of these ineligible and unsupported costs was a result of the owner/management agent ignoring HUD requirements and a lack of effective procedures and controls. The questionable disbursements reduced the amount of project funds available for reasonable and necessary expenses, including maintenance and repair of the projects (see finding 2), and increased the risk of mortgage default.

Identity-of-Interest Contractors Charged the Projects More Than \$1.9 Million in Excessive and Unreasonable Maintenance and Accounting Costs

The owner and management agent did not follow a competitive contracting process when selecting and maintaining contracts with identity-of-interest companies to provide maintenance and accounting services. Although the projects' regulatory agreements and HUD requirements contained in HUD Handbook 4381.5, REV-2, allows for use of identity-of-interest contractors, the cost of services provided by these contractors cannot exceed reasonable rates ordinarily paid for such services on the open market. The handbook also requires the owner to obtain bids for services exceeding \$10,000 per year. However, the owner/management agent did not have procurement procedures and controls in place to adequately ensure the identity-of-interest contractors had to compete with outside companies and, therefore, keep costs reasonable.

Inadequate procurement and bidding information was obtained by the owner/management. The owner/management could not provide bids showing the

identity-of-interest maintenance company competed with other general maintenance contractors when initially selected. In addition, most subsequent bids were obtained for individual services of licensed trades that the identity-of-interest contractor did not employ, and were therefore not comparable. When selecting the identity-of-interest bookkeeping company, resumes were obtained in response to a job add for employment, instead of obtaining bids from contractors. No subsequent attempts were made to verify costs were reasonable. As a result, the projects were charged \$1,562,193 in excessive (ineligible) maintenance costs and \$365,734 in excessive (ineligible) accounting costs.

An Identity-of-Interest Contractor Overcharged the Projects \$1,562,193 for Poor Quality Maintenance Services

Between January 2000 and June 2005, the owner's/management agent's identity-of-interest company, Action Maintenance, charged the projects more than \$3.7 million for maintenance and repair services. We determined that at least \$1,562,193 of these costs were unreasonable, including more than \$1,453,019 in excessive service costs, \$75,674 in direct payroll charges for Action Maintenance's supervisor, and \$33,500 in charges for undocumented unit inspections. Additionally, in violation of the regulatory agreement, the owner/manager allowed an identity-of-interest contractor, Action Maintenance, to improperly mark up the cost of materials purchased for the projects and the cost of repair services provided to the projects by other contractors. Further, serious problems were noted with the quality of the work Action Maintenance claimed to have completed as the work often was not done in a professional manner, was incomplete, and had to be redone, and in some cases, the work apparently was never performed. Maintenance problems were compounded by the owner's and management agent's failure to maintain a work order system to track tenant requests for repairs and related work orders to ensure that tenant service requests were addressed and the necessary work was completed in a professional manner.

Action Maintenance Charged Projects Excessive Rates for Maintenance Services

Between 2000 and 2005, the identity-of-interest contractor billed the projects excessive amounts to address work orders. Action Maintenance charged labor rates of \$30 to \$55 per hour, depending on the employee performing the work. In addition, it charged \$50 or \$65 for an hour or less of service, which was higher than the normal hourly rate. As a result, if an employee worked in one-hour or shorter increments throughout the day, Action Maintenance effectively charged a rate of \$50 to \$260 per hour (the latter representing \$65 per quarter hour). For example, the contractor charged \$65 for 15 minutes of work to place mouse traps (work order 26128 from January 7, 2005). The higher rate was applied even when addressing separate work orders throughout the day for the same project.

Since the employees consistently charged for a full eight hours each day, these high rates may not be considered compensation to Action Maintenance for downtime. According to the management agent, the owner of the projects established the rates charged by its identity-of-interest maintenance company.

Meanwhile, the contractor was only paying its employees salaries of \$8 to \$18 per hour, averaging just over \$11. Personnel files showed the staff were standard maintenance workers with no skilled or licensed carpenters, electricians, or plumbers. The difference between the amounts paid to the employees and the amounts billed to the project was unreasonably high.

A comparison of the amounts charged by the identity-of-interest contractor to rates established in a construction cost index shows Action Maintenance's rates were excessive. We compared the amounts Action Maintenance charged between January 2000 and June 2005 to the standard rates for open shop (nonunion) general laborers documented in Saylor¹ construction cost indexes. The average of the annual base labor rates listed for the Los Angeles area matched the average hourly rate Action Maintenance actually paid its employees. The cost index applied additional amounts for applicable taxes, workers compensation, supervision, overhead, and profit to determine the hourly rate² a contractor should charge to earn a reasonable profit. Based on this information, Action Maintenance should have charged only \$2,248,942 for the more than 89,000 labor hours in question. This is \$1,453,019 lower than the \$3,701,961 Action Maintenance charged the projects, which was 65 percent higher than necessary.

Excessive Maintenance Charges

Housing Project	Amount Charged *	Reasonable Amount	Excessive Amount
Holiday 101-A	\$ 743,263	\$ 465,860	\$ 277,403
Holiday 101-B	\$ 726,036	\$ 439,566	\$ 286,470
Holiday 101-C	\$ 684,314	\$ 412,629	\$ 271,685
Holiday 102	\$ 693,013	\$ 422,757	\$ 270,256
LA Pro 30	\$ 451,067	\$ 269,738	\$ 181,329
Two Worlds II	\$ 404,268	\$ 238,392	\$ 165,876
Total	\$ 3,701,961	\$ 2,248,942	\$ 1,453,019

* Charges up to June 2005

In addition, Action Maintenance's payroll and overhead records showed its actual cost to perform these services was \$1.93 million. Therefore, the contractor received a profit of \$1,763,885 with an excessive profit margin of 48 percent. The excessive profit closely matched the excessive amounts determined through comparison to the standard cost index.

¹ Saylor Publications, Inc. is a California-based publisher of construction and remodeling cost indexes, providing standard information on labor rates and construction costs for contractors and appraisers, updated annually.

² In addition, we added a factor for fringe benefits in line with Action Maintenance's own policies and costs.

The Projects Were Charged Directly for Action Maintenance Supervisor’s Payroll Costs

The management agent and Action Maintenance charged the projects \$75,674 in payroll costs for the supervisor of Action Maintenance between January 2000 and September 2001. These charges were not based on specific work performed by the contractor but allocated to the projects as if he were one of the management agent’s staff performing eligible front-line project activities. However, the supervisor’s payroll was part of Action Maintenance’s overhead costs, already compensated as part of the maintenance billings. Therefore, charging this cost to the projects again represents an ineligible duplicative charge.

Maintenance supervisor cost

Project	2000	2001	Total
Holiday 101-A	\$ 7,110	\$ 6,921	\$ 14,031
Holiday 101-B	\$ 7,110	\$ 6,921	\$ 14,031
Holiday 101-C	\$ 7,414	\$ 7,217	\$ 14,631
Holiday 102	\$ 5,470	\$ 5,324	\$ 10,794
LA Pro 30	\$ 6,138	\$ 5,975	\$ 12,113
Two Worlds II	\$ 5,105	\$ 4,969	\$ 10,074
Total	\$ 38,347	\$ 37,327	\$ 75,674

The Projects Were Charged for Undocumented Unit Inspections

Action Maintenance charged the projects \$33,500 for inspections between May 2003 and May 2005. The invoices were supposed to compensate the contractor for unit inspections performed by the maintenance supervisor. However, these costs were not based on actual work performed. It charged the same amount to each project on consecutive invoices, an apparent allocation of the maintenance supervisor’s payroll (see spreadsheet below). In addition, Action Maintenance did not identify the locations inspected or generate inspection reports to document results. Based on the lack of a work product, poor quality of maintenance by the contractor (as discussed below), and the poor project conditions (see finding 2), it does not appear effective inspections were performed. As a result, these costs were not reasonable and necessary project expenses and, therefore, paid in violation of the regulatory agreement.

Inspection charges

Project	2003	2004*	2005**	Total
Holiday 101-A	\$ 100	\$ 3,250	\$ 2,250	\$ 5,600
Holiday 101-B	\$ 100	\$ 3,250	\$ 2,250	\$ 5,600
Holiday 101-C	\$ 100	\$ 3,250	\$ 2,250	\$ 5,600
Holiday 102	\$ 100	\$ 3,250	\$ 2,250	\$ 5,600
LA Pro 30	\$ 100	\$ 3,250	\$ 2,250	\$ 5,600
Two Worlds II		\$ 3,250	\$ 2,250	\$ 5,500
Total:	\$ 500	\$ 19,500	\$ 13,500	\$ 33,500

* Only charged for second half of 2004

** Costs up to May 2005

Action Maintenance Marked Up Outside Vendor Costs in Violation of HUD Requirements

Action Maintenance marked up costs by up to 35 percent when it purchased materials or used another contractor to perform repairs. The regulatory agreements and HUD Handbook 4381.5 prohibit the owner and management agent from adding surcharges to actual costs. The fiscal year 2000 financial audits for the projects³ identified a reportable condition on internal controls, stating Action Maintenance charged a 33.3 percent markup on material purchases. In addition, we identified examples of 35 percent markups added to work performed by outside contractors in 2002. Due to the management agent's and maintenance contractor's inadequate record keeping, we could not determine the total excessive amount charged.

Maintenance Work Was Unsatisfactory Due to the Owner's/Management's Failure to Monitor Maintenance

Review of maintenance work performed on a sample of units showed work was not completed in a professional manner. Our inspections on 60 sample units (see finding 2) showed 328 (36 percent) of the work order repairs performed since 2003 were questionable, including poor quality repairs, incomplete work, repeated repairs, questionable lock repairs, unsupported work, and other similar issues. These conditions were allowed to occur due to the owner's and management agent's failure to monitor the contractor's work and to establish procedures and controls over maintenance and inspections. These matters resulted in the projects being charged for unreasonable work and necessary repairs not being fully resolved.

- Action Maintenance's quality of work was inadequate.

The contractor charged the projects for 26 work orders despite unacceptable workmanship.

Example 1. For Holiday 101-C unit D304 and LA Pro 30 unit B209, the contractor performed shower repairs. This work was charged to the projects respectively in December 2004 under invoice 33228 for \$110 and in March 2004 under invoice 25604 for \$55. However, our June 2005 inspection of these units found, as part of the repair, the shower heads had been removed without installing new ones, leaving the pipe bare (see photograph of shower).

³ Financial audits for Holiday 101-A, 101-B, 101-C, LA Pro 30, and Two Worlds II included the condition, but the audit for Holiday 102, with a different fiscal year end date, did not.



Example 2. On December 2, 2003 Action Maintenance verified a window had fallen out and broken in LA Pro 30, 1606 West 47th, unit F111, and two windows needed to be replaced. However, work did not begin until December 17, 2003, performed under four work orders. On January 26, 2004, additional work was performed under work orders 16127 and 16114. Overall, only two of at least three windows needing replacement had been replaced. Our physical inspection on June 7, 2005, a year and a half later, showed the frames had not been installed, and the exterior wood was left exposed (see exterior photograph). In addition, the windows would not open properly and were not sealed, which allowed water to get in. This work was performed by three of Action Maintenance's most experienced long-term employees. The labor cost alone for this poor quality repair was \$1,132.



- Action Maintenance left work incomplete.

Action Maintenance did not perform all the work necessary to fully resolve and complete 17 work orders. For example, bathroom work was performed by the contractor on Two Worlds II, 474 Hartford, unit B09, on June 8, 2005. However, the work was still incomplete as of our June 21, 2005, inspection (see photograph of bathroom ceiling), and appears to have remained so at least until November 2005. In addition, Action Maintenance poorly patched a section of the ceiling by placing drywall over the existing drywall ceiling.



- Action Maintenance had to repeat its repairs.

There were 69 work orders in which Action Maintenance had to revisit and recharge the project to resolve the same issue. Information showed the contractor had been unable to properly address the problem on its first attempt, which resulted in the projects incurring additional costs. If qualified tradesmen had performed the work, the problem could have been immediately resolved and resulted in lower overall charges.

For example, LA Pro unit C108 had a kitchen sink faucet leak repair in January 2004 under work order 16125. The leak was not fixed, and the repair had to be repeated in March 2004 under work orders 17520 and 17428 and then again in June 2004 under work order 19361. It was not fixed until December 2004 under work order 26699. This work was performed by three of Action Maintenance's most experienced, long-term employees for a total cost of \$297 to the project for labor alone. This same unit also had the

garbage disposal removed and fixed in January 2004, which had to be done again in March 2004. In addition, the toilet wax ring was replaced in January 2004 but had to be replaced again in April 2004 because it was leaking.

- Action Maintenance charged for questionable lock repairs.

There were 101 work orders for lock repairs and similar work that did not appear reasonable and necessary due to their unusual frequency on the same units. For example, LA Pro 30 unit B203 had 11 work orders to repair entrance door locks between January 2004 and May 2005, costing the project \$605. The tenant occupying the unit since 1996 had no knowledge of this work. In addition, Holiday 101-C unit B305 had 12 work orders between April 2003 and November 2004 to repair the entrance door locks and program phone numbers into the intercom, costing the project \$642. Since on-site managers have copies of the keys for lockouts, it isn't clear whether this work was necessary or performed.

- The management agent could not produce all work orders.

We requested all invoices and work orders associated with maintenance work performed since 2003 on the units inspected. Although most invoices and work orders were available, documentation for 97 separate charges to the projects was missing. The only information available was invoice data in the management agent's Quickbooks accounting system. As a result, we could not determine exactly what was done or who performed the work.

- Action Maintenance also charged for other questionable work.

Nineteen work orders included various issues making the work performed appear questionable. For example, repairs to LA Pro 30 unit F111 under work order 9390 stated that a paper holder rack was replaced as of January 2003 for \$50. However, as of our June 2005 inspection, there was no applicable paper holder rack in the unit.

The owner and management agent did not monitor maintenance performed by Action Maintenance to ensure the work was properly completed. They did not require the identity-of-interest contractor to implement a satisfactory maintenance work order system to ensure all necessary repairs were adequately addressed. There was no log to identify and track tenant requests or deficiencies identified during inspections. In addition, there was no system to ensure work orders were completed within a reasonable timeframe for a reasonable cost. There was also no evidence the maintenance supervisor evaluated the performance of the staff or verified the skills of new employees. Although the maintenance supervisor was a licensed contractor, he was inexperienced at running a maintenance company.

Action Maintenance's lack of tracking, monitoring, and evaluating repairs compounded problems with its questionable work product.

Identity-of-Interest Contractors Charged the Projects Unreasonable and Duplicative Fees for Accounting Services

The owner and management agent contracted with two identity-of-interest contractors, Action Bookkeeping and Accounting Data Systems, to provide accounting services for the projects. Although HUD allows a management agent to charge for accounting services it provides, it has established a maximum allowable fee for these services of \$7.50 per unit per month. The \$366,474 in fees the projects paid the identify-of-interest accounting firms from December 2000 through November 2004 exceeded this cap by \$144,714.

In addition, during the period from August 2001 through November 2004, the management agent charged the projects \$221,019 for the direct time of two of its staff for providing accounting services to the projects. By charging for services through a vendor and then again directly, the management agent double charged the projects for accounting services. Overall, as summarized below, the \$365,734 paid by the projects in excess of the HUD-established fee cap represents ineligible project expenses. There is no evidence the owner of the projects fulfilled his responsibility to ensure the charges were reasonable by taking steps to limit the accounting costs.

Excessive/duplicative bookkeeping charges

Projects	2001	2002	2003	2004	Total
Holiday 101-A	13,941	19,375	17,766	18,694	\$ 69,776
Holiday 101-B	13,941	19,375	17,766	18,694	\$ 69,776
Holiday 101-C	14,537	20,203	18,525	19,493	\$ 72,758
Holiday 102	3,342	14,903	13,666	14,380	\$ 46,291
LA Pro 30	10,290	16,725	15,336	16,138	\$ 58,489
Two Worlds II	8,558	13,910	12,755	13,421	\$ 48,644
Total	\$ 64,609	\$104,491	\$ 95,814	\$100,820	\$ 365,734

Payroll Costs of the Management Agent's President Were Charged to the Projects

The management agent inappropriately charged the projects \$380,670 in payroll costs for its president. Such charges are considered management agent costs and under the terms of the applicable regulatory agreements and HUD guidelines, are not eligible for payment from project funds. The payroll costs charged to the

projects ranged from 60 to 70 percent of the president's total salary and related costs, including salary, bonus, taxes, and workers compensation through September 2004, when the charges abruptly stopped.

Although HUD Handbook 4381.5, REV-2, does allow an agent to charge projects for front-line staff, it also states that management agents must cover the cost of supervising and overseeing project operations out of their management agent fee. Activities already compensated through the fee include supervising project personnel, monitoring project operations through site visits, analyzing and solving project problems, designing procedures and systems, etc. The president's job description included supervisory functions, such as overseeing staff, reviewing correspondence, setting policies/procedures, overseeing occupancy, approving payroll reports, acting as liaison with HUD, reporting to owners, visiting properties, etc. Clearly, these functions are management agent duties, the cost of which is to be covered by the management fee. Charging the projects again for functions the projects were already paying for through the management fee represents an ineligible duplicative charge.

President's ineligible payroll

Project	2000	2001	2002	2003	2004	Total
Holiday 101-A	\$ 14,680	\$ 14,843	\$ 14,868	\$ 14,829	\$ 11,364	\$ 70,584
Holiday 101-B	\$ 14,680	\$ 14,843	\$ 14,868	\$ 14,829	\$ 11,364	\$ 70,584
Holiday 101-C	\$ 15,308	\$ 15,477	\$ 15,503	\$ 15,463	\$ 11,849	\$ 73,600
Holiday 102	\$ 11,292	\$ 11,417	\$ 11,437	\$ 11,407	\$ 8,742	\$ 54,295
LA Pro 30	\$ 12,672	\$ 12,813	\$ 12,835	\$ 12,801	\$ 9,810	\$ 60,931
Two Worlds II	\$ 10,540	\$ 10,656	\$ 10,674	\$ 10,647	\$ 8,159	\$ 50,676
Total	\$ 79,172	\$ 80,049	\$ 80,185	\$ 79,976	\$ 61,288	\$ 380,670

Questionable Office Rental and Capital Improvement Costs Totaling \$350,321 Were Charged to the Projects

The management agent charged the projects \$209,441 for rent of and \$140,880 for capital improvements to the management agent's central office in violation of the projects' regulatory agreements and HUD requirements. HUD Handbook 4381.5, REV-2, does allow management agents to charge office costs for employees performing front-line activities to the projects. However, the amount charged by the management agent did not represent an appropriate allocation of the actual costs and covered the cost of space not necessary for the eligible front-line personnel, including the general partner's offices. As a result, a portion of the rent and capital improvements would not be reasonable and necessary in accordance with the regulatory agreement.

The central office only occupied a limited portion of the first floor of a two-story building and shared this space with the identity-of-interest maintenance contractor and accounting companies. The second floor also included the general partner's principal place of business. In addition, the management agent managed the operations of three to five additional non-HUD projects between 2000 and 2004, which should also be allocated some of the costs. However, the amount charged to the six HUD projects was more than 75 percent of the entire building's \$60,000 annual rental cost, an unreasonable amount. The questionable rental costs paid by the projects are summarized below.

Agent's office rent

Project	2000	2001	2002	2003	2004	Total
Holiday 101-A	\$ 8,970	\$ 8,622	\$ 8,622	\$ 7,905	\$ 7,902	\$ 42,021
Holiday 101-B	\$ 8,970	\$ 8,622	\$ 8,622	\$ 7,905	\$ 7,902	\$ 42,021
Holiday 101-C	\$ 9,353	\$ 8,990	\$ 8,989	\$ 8,239	\$ 8,239	\$ 43,810
Holiday 102	\$ -	\$ 9,396	\$ 6,633	\$ 6,083	\$ 6,083	\$ 28,195
LA Pro 30	\$ -	\$ 7,443	\$ 7,442	\$ 6,820	\$ 7,440	\$ 29,145
Two Worlds II	\$ -	\$ 6,190	\$ 6,191	\$ 5,676	\$ 6,192	\$ 24,249
Total	\$ 27,293	\$ 49,263	\$ 46,499	\$ 42,628	\$ 43,758	\$ 209,441

In addition, capital improvement charges performed on the central office are questionable. Over 70 percent of these costs were allocated to the projects, which included all costs attributable to common areas, even though utilized by the management agent and maintenance contractor. In addition, it included all space utilized by management agent staff who did not work exclusively on the projects, as well as, space for ineligible staff such as the management agent's President (see finding above). In fact, the only space designated for Proland management's office space was one-half of the President's and Controller's offices.

Capital improvements

Project	2000	2001	Total
Holiday 101-A	\$ 23,794	\$ 2,280	\$ 26,074
Holiday 101-B	\$ 24,202	\$ 2,280	\$ 26,482
Holiday 101-C	\$ 26,655	\$ 2,378	\$ 29,033
Holiday 102	\$ 18,702	\$ 1,697	\$ 20,399
LA Pro 30	\$ 20,901	\$ 182	\$ 21,083
Two Worlds II	\$ 17,656	\$ 153	\$ 17,809
Total	\$ 131,910	\$ 8,970	\$ 140,880

Currently, there is insufficient information to show what portion of these charges were for reasonable and necessary office space costs required for eligible front-line staff to perform their project responsibilities.

Holiday Apartments Paid the Owner's Expenses

Between 2001 and 2004, Holiday Apartments paid \$21,600 in ineligible ownership franchise taxes. These taxes were the responsibility of the individual partners of the ownership entities and should not have been paid from project funds. The projects' regulatory agreements require that project funds be used only to pay for reasonable project expenses.

This matter was identified in the fiscal year 2001 financial audit reports, which stated a bookkeeping error resulted in the projects mistakenly paying these amounts from the project funds and stated the amounts had been repaid. However, after 2001, the projects continued to pay these ineligible costs each year. The matter was again identified as a condition on the fiscal year 2004 financial audit reports.

Review of the projects' general ledgers and related support showed that in December 2002 and February 2005, the management agent returned \$10,400 of these ineligible expense payments to the projects. However, \$11,200 had not been reimbursed to the projects, as follows:

Ineligible franchise taxes

Property	Franchise tax paid for	2002	2003	2004	Total
Holiday 101-A	Holiday A limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 101-A	Wilshire Holiday A limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 101-B	Holiday B limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 101-B	Wilshire Holiday B limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 101-C	Holiday C limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 101-C	Wilshire Holiday C limited	\$ 800	\$ 800	\$ -	\$ 1,600
Holiday 102	West Holiday 102	\$ -	\$ 800	\$ 800	\$ 1,600
Total		\$ 4,800	\$ 5,600	\$ 800	\$ 11,200

Projects Continue to Pay for Similar Inappropriate Expenses

The maintenance, accounting, management office rent, and inspection costs were ongoing issues, extending beyond the period of our review. We anticipate these issues resulted in additional ineligible and unsupported charges to the projects. Overall, we estimate that after our audit period, through December 2005, the projects would have been charged \$457,444 in additional ineligible and unsupported costs, including \$264,185 for one year of maintenance, \$100,374 for one year of bookkeeping, \$76,135 for one year of rent, and \$16,750 for six months of inspection costs.

The Owner/Management Knew Costs Were Inappropriate

The owner and management agent knew about problems with the excessive and ineligible costs since 2001. The 2000 financial audit reports for the projects, issued in 2001, included findings that charges to the projects for the management agent's president, the maintenance supervisor, and capital improvements on the management agent's office were unreasonable. The reports also identified a reportable condition on internal controls over maintenance, which stated there were no organization policies or procedures, maintenance records were inadequately maintained, errors and duplicate charges were noted, and no receiving reports were obtained from managers or tenants to show the job was done or appliances received. In addition, there was no schedule for preventive maintenance, invoices were not checked by the supervisor, and the costs appeared excessive. Despite knowledge of these conditions, no efforts were made by the owner to curb excessive and ineligible costs by its identity-of-interest companies.

Due to a lack of independence, the management agent did whatever the owner of the projects wanted, even to the detriment of the projects. The president and controller of the management agent also held these same positions with the identity-of-interest company providing the maintenance and bookkeeping services. When issues over maintenance were brought to the attention of the president of the management agent, he stated that he had no control and all decision making was done by the ownership, including the general partner of the projects, and although he was the president, he was still just an employee.

Conclusion

Overall, the owner ignored HUD requirements by charging more than \$2.6 million in ineligible and unsupported costs to the projects through his identity-of-interest companies. The inappropriate charges and poor maintenance work could have been prevented through the establishment of strong procedures and controls in compliance with HUD requirements. However, the ineligible and unsupported charges benefited the owner by increasing the profits of these companies in which he had ownership interest, leaving little incentive to ensure only reasonable amounts were charged, and as a result, the owner did not establish effective controls. Due to the lack of independence, the owner of the projects was able to set the inappropriate practices and was, therefore, directly responsible for the activity of these companies. As a result, the projects were left in poor financial condition, increasing the risk of mortgage default, and the properties were not maintained in appropriate condition (see finding 2).

Recommendations

We recommend that the director of HUD's Los Angeles Multifamily HUB require the project owner/management agent to

- 1A. Develop and implement written procurement, contracting, and disbursement policies and procedures acceptable to HUD.
- 1B. Terminate the use of Action Maintenance, Action Bookkeeping, and Accounting Data Systems and contract maintenance and accounting services with independent third parties.
- 1C. Pay from non project funds the excessive identity-of-interest maintenance costs of \$1,453,019 to the projects' respective reserve for replacement accounts.
- 1D. Pay from non project funds the payroll costs of \$75,674 for the contractor's maintenance supervisor to the projects' respective reserve for replacement accounts.
- 1E. Pay from non project funds the inspection charges of \$33,500 to the projects' respective reserve for replacement accounts.
- 1F. Identify all surcharges on materials and third-party contractors added on by Action Maintenance and pay from nonproject funds the inappropriate amounts to the projects' respective reserve for replacement accounts.
- 1G. Pay from non project funds the excessive and duplicative identity-of-interest accounting/ bookkeeping of \$365,734 to the projects' respective reserve for replacement.
- 1H. Pay from non project funds the \$380,670 in payroll costs of the management agent's president to the projects' respective reserve for replacement accounts.
- 1I. Provide support to show what portion of the \$209,441 in office rent was reasonable or pay the projects' respective reserve for replacement accounts from non project funds.
- 1J. Provide support to show what portion of the \$140,880 in capital improvement costs was reasonable or pay the projects' respective reserve for replacement account from nonproject funds.
- 1K. Pay from nonproject funds the ineligible ownership costs of \$11,200 to the projects' respective reserve for replacement accounts.

1L. Submit documentation to identify maintenance costs billed to the projects after June 2005 and bookkeeping/accounting and management agent office rent billed to the projects after December 2004 for HUD to determine the ineligible amounts and the owner to pay from non project funds the ineligible amounts to the projects' respective reserve for replacement accounts.

1M. Impose civil money penalties and pursue double damages remedies against the projects' general partner and management agent under the applicable equity skimming statutes in conjunction with the OIG.

Finding 2: The Projects Were Not Maintained in Good Repair and Free of Health and Safety Violations

The owner did not maintain Holiday Apartments (101-A, 101-B, 101-C, and 102), LA Pro 30, and Two Worlds II free of health and safety violations. Inspections of statistically selected units and their associated buildings showed 50 of 60 Section 8 units and all 25 buildings did not meet HUD’s housing quality standards. Overall, we estimate \$561,600 in housing assistance payments were made for properties in material violation of HUD quality standards. These conditions occurred due to the owner/management not ensuring the properties were adequately maintained by the identity-of-interest maintenance contractor. Consequently, tenants had to live in units and buildings that were not decent, safe, and sanitary.

Project Units Were Not Decent, Safe, and Sanitary

Our inspection of a statistical sample of 60 units and their 25 associated scattered-site buildings identified 166 24-hour health and safety violations, 14 10-day violations, and 60 30-day violations (see appendix C for sampling methodology and appendix D for results by building and unit). HUD requirements under 24 CFR [*Code of Federal Regulation*] 5.701 and 5.703 state that owners of HUD-insured projects and facilities with project-based Section 8 funding must maintain the dwelling units, site, building systems, and common areas free of health and safety hazards and in good repair. In addition, according to HUD Handbook 4381.5, chapter 6, assisted units must comply with housing quality standards or local housing codes, whichever are more stringent. The violations resulted in 100 percent of the buildings and 83 percent of the units reviewed failing housing quality standards under 24 CFR [*Code of Federal Regulations*] Part 982.

Inspection results

Project	Buildings	Units	Violations
Holiday 101-A	5	10	44
Holiday 101-B	5	12	44
Holiday 101-C	4	16	63
Holiday 102	2	5	26
LA Pro 30	5	9	37
Two Worlds II	4	8	26
Total	25	60	240

The results of our inspection were previously provided to HUD and to the projects’ management agent. Some of the most significant and/or prevalent violations included the following:

Frequency of violations

Issue	24-hour violations	10-day violations	30-day violations	All violations
Inoperable/disconnected smoke detector	13	0	0	13
Inoperable/damaged stove/range	13	0	1	14
Gas leak	1	0	0	1
Inoperable/damaged water heaters and furnaces	16	4	4	24
Blocked emergency egress	10	0	0	10
Electrical hazards	20	3	2	25
Damaged/moldy/rotted bathroom	4	0	10	14
Damaged refrigerator	9	0	4	13
Tripping/falling hazard	5	0	5	10
Potential landslide danger	0	0	1	1
Excessive buildup of debris, filth, or foreign materials	26	0	4	30
Elevators not working properly	4	0	0	4
Broken/missing/poorly fitting window glass	2	2	4	8
Insecure/missing handrails	3	0	1	4
Rotted/unsafe balconies and landings	2	0	3	5
Other	38	5	21	64
Total violations	166	14	60	240

The photographs below illustrate some of the conditions we found in the project units and buildings.

Location: Two Worlds II, 1228 Kingsley, unit C06



Cracked stove

Location: LA Pro 30, 817 Parkview, unit D106



Tub wall separating and deteriorating

Location: Two Worlds II, 420 Union



Detached handrail in common area

Location: Holiday 101-B, 106 Commonwealth



Furnace exhaust not ventilating to exterior of building.

In addition, our earlier cursory review of Holiday Apartments building exteriors in March 2005 identified several significant problems, such as a deteriorated egress door, exposed electrical wiring, missing fire extinguisher, loose railing, rotted window frames, etc.

Location: Holiday 101-A, 1107 West 42nd Street



Damaged roof access door

Violations Were Caused by the Owner's Neglect and Lack of Controls over Maintenance

The violations were generally long term in nature, and many were caused by the owner ignoring HUD requirements and neglecting the properties for long periods. The owner did not establish effective procedures to monitor the maintenance work, perform preventive maintenance, or perform and document inspections (see finding 1), and these deficiencies contributed to the high number of violations.

The owner's and management agent's failure to correct deficiencies identified during HUD's Real Estate Assessment Center inspections demonstrated the owner's neglect and disregard for HUD requirements. As part of our unit inspections and review of work orders, we checked violations identified as part of prior HUD Real Estate Assessment Center inspections. There were two instances in which deficiencies had not been addressed and four instances in which the problems were not addressed in a reasonable amount of time. For example, the HUD Real Estate Assessment Center's May 2003 inspection of Holiday 101-C unit C-216 identified problems with the garbage disposal and refrigerator. There was no evidence the garbage disposal was repaired until July 2004, 14 months later. In addition, there were no work orders generated to fix the refrigerator, which was again identified as a violation during our June 2005 inspection. These problems were not addressed due to the lack of maintenance procedures and controls to ensure deficiencies were properly recorded, tracked, and completed (see finding 1).

Section 8 Funds Were Paid for Units in Material Violation

Based on the inspection results, all of the units sampled would have failed HUD's Section 8 housing quality standards through the unit interior and/or building inspections, since common area violations impact all units within the building. Adjusting for the severity of the violations, 32 units inspected and another 124 Section 8 units within five of the buildings with the most severe violations materially violated housing requirements. As a result, \$561,600⁴ in housing assistance payments was paid between July 2004 and June 2005 to house tenants in units and buildings not meeting HUD requirements.

⁴ Based on average annual housing assistance payments for 156 units.

Recommendations

We recommend that the director of HUD's Los Angeles Multifamily HUB

2A. Require the owner to correct all violations identified, which resulted in \$561,600 in housing assistance payment to units and buildings not meeting HUD's requirements, and certify to HUD that the violations have been resolved.

2B. Perform followup inspections of the six properties to ensure they are decent, safe, and sanitary.

2C. Develop and implement written maintenance, repair, and inspection policies and procedures acceptable to HUD to ensure the properties are maintained free of housing violations.

Finding 3: The Owner and Management Agent Mismanaged the Projects

The owner and management agent did not manage the projects in a reasonable manner. They failed to ensure identity-of-interest maintenance and accounting services were reasonable; charged the projects for ineligible amounts; failed to maintain the projects free of health and safety violations and in good repair; did not maintain an inventory; and did not accurately calculate, report, and resolve \$655,173 in project liabilities, including excess income, reserve for replacement, payables to the City of Los Angeles, and a note payable. These problems occurred due to the lack of procedures and controls, failure to maintain documentation, and the use of identity-of-interest contractors. As a result, the projects were left in poor physical and financial condition, critical information was not reported accurately, and the risk of default on the HUD-insured mortgages increased.

Management Did Not Ensure Maintenance and Accounting Services were Reasonable

The management agent did not sufficiently supervise or control the activities of the identity-of-interest maintenance and accounting contractors. As discussed in finding 1, the management agent did not follow HUD requirements over procurement to prevent excessive costs and failed to ensure quality work was performed by the maintenance contractor.

Management Charged Ineligible and Unsupported Costs to Projects

The management agent charged the projects for costs already paid through their management fees, including the president's salary and unknown portions of the central office costs (see finding 1). Unreasonable amounts paid to the management agent would benefit the projects' general partner, through his ownership of the management agent.

Management Did Not Ensure Projects Were in Good Repair

The owner and management agent did not operate the projects in a manner ensuring they were maintained in good repair as required by the regulatory agreements and other HUD criteria. Numerous health and safety violations were

identified during our sample inspections (see finding 2). In addition, both Holiday 101-A and Holiday 101-B failed recent HUD Real Estate Assessment Center physical inspections.

Management Failed to Maintain an Accurate Inventory

The management agent did not have an accurate inventory of project appliances and equipment. It never developed formal procedures to track the placement of project assets. The president of the management agent informed us the management agent trusted the maintenance contractor's employees to know where the project assets were located. The regulatory agreements require that records over project equipment be maintained in reasonable condition for proper audit. An inventory is necessary to audit equipment, including appliances. In addition, HUD Handbook 4350.1, chapter 4, requires the owner to provide HUD with information on changes or replacement of appliances and items that are normally identified by make, model, and serial number. When questioned about these practices, the management agent informed us that at one point, it tried to get the inventory under control but the ownership, including the general partner of the projects, prevented it.

We reviewed all available sources of information showing the location of the projects' assets. The management agent could only produce an undated and unsigned hand-written list of recently purchased appliances, identifying their unit location, although it did not include information on older appliances. Invoices and general ledger entries for appliance purchases sometimes mentioned where items were delivered. Work orders mentioned when Action Maintenance installed or removed the items. However, in no cases were the appliances identified by serial number, and when they were moved out of a unit, there was no indication of where they were taken.

As part of unit inspections, we attempted to confirm 16 recently purchased appliances identified in the available documentation. However, not all items could be confirmed, and comparison of the management agent's handwritten list to the general ledgers, invoices, and work orders showed various discrepancies. The general ledger, invoices, and/or work orders listed the installation of four appliances that the management agent's list failed to identify, two of which could be confirmed in the units. In two cases, the management agent listed a stove going into the unit when it was actually a refrigerator. Also, due to a lack of serial numbers, we could not confirm two items on the agent's list and an additional item in the general ledger to the applicable unit. Finally, due to discrepancies between the agent's list and the general ledger, it was unclear whether one or two refrigerators were moved in and out of a unit, but in either

case, there was no information as to where they were taken afterward. Overall, the management agent’s inventory tracking was inaccurate and insufficient. As a result, it is not clear whether all items purchased by the projects are actually at the properties.

Management Failed to Correctly Report Excess Income

The general partner and management agent failed to ensure the projects accounted for excess income amounts due to HUD. This violated the Housing Act of 1937, section 236, which requires the projects to provide monthly reports of excess income collected from tenants for charges over the base rent. These funds are to be remitted to HUD unless HUD authorizes the projects to retain them.

Between 2000 and 2004, the management agent only submitted 109 of the 240 monthly excess income reports required. This problem continued after the fiscal year 2000 financial audit reports identified the nonsubmission of the reports as a finding, which remained an outstanding issue through 2001. Although HUD granted waivers on the payments for Holiday 101-A, 101-B, and 101-C during certain periods, allowing the excess income to be placed in the reserve for replacement accounts, the reports were still required. The actual payments to HUD and the reserve totaled \$7,038, and many of the available reports listed zero excess income.

During our confirmation of excess income calculations, the management agent admitted previous reports had been incorrectly prepared to reflect zero excess income. In March 2005, the agent submitted corrected reports for the period 2002 to 2004. Based on these revised reports, the projects must remit an additional \$13,018 to HUD and \$7,166 to the reserve for replacements, as follows:

Corrected monthly reports of excess income

Property	Revised reports 2002 - 2004	Funds due to HUD	Funds due to reserve for replacement	Totals
Holiday 101-A	24	\$2,376	\$1,207	\$3,583
Holiday 101-B	24	4,135	4,945	9,080
Holiday 101-C	24	3,069	1,014	4,083
Holiday 102	41	3,438		3,438
Total	113	\$13,018	\$7,166	\$20,184

The lack of reporting and incorrect information appear to be due to the lack of effective procedures and controls to ensure accurate and timely reporting to HUD.

**Delinquent Reserve Funds
Were Not Reported or Paid**

The owner and management agent failed to ensure the projects repaid funds borrowed from the reserve for replacement accounts. The regulatory agreements require monthly payments to the reserve for replacement, to be used for major project repairs and released with HUD’s approval. HUD allowed the four Holiday projects to borrow \$705,681 from their reserve accounts between August 1999 and December 2004 to cover operations when Section 8 subsidy payments were delayed and to pay insurance costs.

The fiscal year 2000 financial audit reports for Holiday 101-A, 101-B, and 101-C identified the borrowed funds as overdue, which remained outstanding through November 30, 2001. The outstanding balances were again identified as conditions on the fiscal year 2004 financial audit reports for Holiday 101-A and 101-B.

After management submitted documentation regarding various project repairs, HUD waived the majority of the amount owed between November 2001 and March 2002. In addition, Holiday 101-C and 102 returned \$81,907 to their reserves between December 2004 and May 2005. However, \$129,142 was still owed to the project reserves, as follows:

Delinquent amounts owed to reserve for replacement account

Property	Borrowed	Repaid	HUD allowed offset	Total owed
Holiday 101-A	\$ 237,633	\$ -	\$ 158,234	\$ 79,400
Holiday 101-B	\$ 147,252	\$ -	\$ 124,880	\$ 22,372
Holiday 101-C	\$ 169,599	\$ 25,606	\$ 144,008	\$ (15) *
Holiday 102	\$ 151,197	\$ 56,301	\$ 67,525	\$ 27,370
Total	\$ 705,681	\$ 81,907	\$ 494,647	\$ 129,142

* Amount repaid and offset exceeds balance borrowed, but doesn't impact balance other project's owe.

Although we did not review the detail for LA Pro 30 and Two Worlds II, the fiscal year 2004 financial audit reports identified similar outstanding balances of \$12,264 and \$8,164, respectively.

**Management Did Not Address
Obligations to the City of Los
Angeles**

The owner and management agent did not take appropriate action to resolve outstanding obligations to the City of Los Angeles for systematic code enforcement ordinance and rent stabilization inspections. Holiday Apartment

payables due to the City of Los Angeles⁵ totaling \$115,841 have been outstanding since 2000. The lack of payment resulted in the assessment of substantial late charges, which are ineligible since they are not reasonable and necessary project expenses. Holiday 101-B also received a final notification letter from the city, threatening to take legal remedies, which may include liens or seizure of the property. As of the October 22, 2004, invoices, the obligation balances were as follows:

Amounts owed to City of Los Angeles

Property	Outstanding charges	Late fees assessed	Total amount due
Holiday 101-A	\$ 19,957	\$ 11,358	\$ 31,315
Holiday 101-B	\$ 27,540	\$ 19,004	\$ 46,544
Holiday 101-C	\$ 11,266	\$ 7,214	\$ 18,480
Holiday 102	\$ 12,323	\$ 7,179	\$ 19,502
Total	\$ 71,086	\$ 44,755	\$ 115,841

These matters were not included in the account payable balances or notes in the projects' financial statements submitted to HUD. According to the management agent, it did not inform the project's financial auditing firm about the delinquent amounts. The owner's and agent's inactivity and failure to report significant matters resulted in unnecessary late charges and put the HUD-insured properties at risk.

The Project Is Missing Support for Note Payable

The financial statements for Holiday 101-B include a questionable note payable for \$369,578. According to the management agent, this amount is supposed to be an earthquake loan from HUD. However, management could not provide support or identification numbers showing the legitimacy of the note. As a result, it is not clear whether this is an eligible project payable.

Conclusion

The owner and management agent demonstrated poor management through their failure to control project disbursements, safeguard project assets, maintain the properties in good repair, and report critical information to HUD. The mismanagement stemmed from the owner's and management agent's failure to establish effective policies and procedures, including those for excess income,

⁵ We did not review whether similar amounts were due from LA Pro 30 or Two Worlds II.

inventory, and document maintenance to ensure the projects were in compliance with HUD requirements. The identity-of-interest relationship between the management agent and major contractors resulted in a lack of independence. As a result, the projects were left in poor financial and physical condition. These issues can only be resolved through the repayment of project funds, establishment of procedures and controls, and removal of identity-of-interest contractors, including the management agent.

Recommendations

We recommend that the director of HUD's Los Angeles Multifamily HUB

- 3A. Take appropriate administrative action against the management agent and the projects' ownership, including requiring the owner to remove Proland Management Company as the projects' management agent and obtain a new independent management management agent acceptable to HUD.
- 3B. Require the projects to develop and implement written inventory, excess income, and document maintenance policies and procedures.
- 3C. Require the projects to remit excess income owed to HUD of \$13,018 and submit \$7,166 to the applicable replacement reserves.
- 3D. Require the projects to return the \$149,570 in borrowed funds to their respective reserve for replacement accounts.
- 3E. Require the owner to address the \$115,841 obligation to the City of Los Angeles and report amounts owed in the financial statements. If the city does not waive the \$44,755 in late fees, we recommend HUD require the owner to pay these expenses.
- 3F. Provide support as to the legitimacy of the \$369,578 note payable.

SCOPE AND METHODOLOGY

We performed our review at HUD's Los Angeles regional office and the management agent's offices from January to October 2005. To accomplish our objectives, we interviewed HUD officials, management agent staff and officials, and the general partner. The primary methodologies included

- Reviews of the projects' regulatory agreements and management agent certifications.
- Reviews of applicable HUD guidance, including HUD handbook and *Code of Federal Regulations* requirements.
- Reviews of HUD's referral documentation and monitoring files, including monitoring reviews, correspondence, mortgage documentation, housing assistance payment documents, and Real Estate Assessment Center inspection results.
- A walk-through on a nonstatistical sample of seven scattered-site building exteriors in March 2005 to generally assess the properties' physical conditions.
- Inspecting a statistical sample of 60 of 609 project-based Section 8 units in June 2005 to determine whether they met health and safety standards (see appendix C for sampling methodology). We also inspected the associated exterior and common areas of 25 out of 29 scattered-site buildings. In addition, we reviewed and confirmed work order information for each unit inspected for the period January 2003 to May 2005. We interviewed available tenants and confirmed recently installed appliances.
- Reviews of the projects' annual audited financial statements from 2000 to 2004.
- Reviews of the projects' financial records, such as invoices, payroll, bank reconciliations, and general ledgers, including downloads from the management agent's Quickbooks accounting system.
- Reviews of standard cost index information from 2000 to 2005.

The review generally covered the period of January 1, 2000, to December 31, 2004. This period was adjusted as necessary. We conducted our 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 that management has in place to reasonably ensure that HUD-insured projects are administered in accordance with regulatory agreements and HUD requirements.

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 projects lacked effective procurement, contracting, and disbursement procedures and controls to reasonably ensure project funds were used in compliance with the regulatory agreement and HUD requirements (see findings 1 and 3).
- The projects lacked effective maintenance and inspection procedures and controls to ensure the projects were maintained in a reasonable condition and free of health and safety defects (see findings 1, 2, and 3).

- The projects lacked effective controls over the use, supervision, and monitoring of identity-of-interest contractors (see findings 1, 2, and 3).
- The projects lacked effective controls to ensure proper reporting to HUD (see finding 3).

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/
1C	\$1,453,019		\$264,185
1D	\$75,674		
1E	\$33,500		\$16,750
1G	\$365,734		\$100,374
1H	\$380,670		
1I		\$209,441	\$76,135
1J		\$140,880	
1K	\$11,200		
2A			\$561,600
3C	\$13,018		\$7,166
3D			\$149,570
3E	44,755		\$71,086
3F		\$369,578	
Total	\$2,377,570	\$719,899	\$1,246,866

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 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/ “Funds to be put to better use” are quantifiable savings that are anticipated to occur if an OIG recommendation is implemented, resulting in reduced expenditures at a later time for the activities in question. This includes costs not incurred, deobligation of funds, withdrawal of interest, reductions in outlays, avoidance of unnecessary expenditures, loans and guarantees not made, and other savings.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

<p>Comment 1</p>	<p style="text-align: center;">Holland & Knight</p> <p style="text-align: center;">Tel 202 955 3000 Fax 202 955 5564</p> <p style="text-align: right;">Holland & Knight LLP 2099 Pennsylvania Avenue, N.W. Suite 100 Washington, D.C. 20006 www.hklaw.com</p> <p style="text-align: right;">Stephen D. Niles 202 457 7017 stephen.niles@hklaw.com</p> <p>February 21, 2006</p> <p><u>VIA ELECTRONIC MAIL AND FEDERAL EXPRESS</u></p> <p>Ms. Joan S. Hobbs Regional Inspector General for Audit U.S. Department of Housing and Urban Development Office of Inspector General Region IX 611 West Sixth Street, Suite 1160 Los Angeles, California 90017-3101</p> <p>Dear Ms. Hobbs:</p> <p>On behalf of my firm's client, the general partner of the owners (the "Owners") of Holiday Apartments (101-A, 101-B, 101-C and 102), Two Worlds II and LA Pro 30 (collectively, "the Projects"), we are submitting this response (the "Response") to your letter to the general partner, dated January 19, 2006, and the accompanying discussion draft audit report (the "Draft Report"). As discussed in detail below, the allegations made by the Office of Inspector General ("OIG") in the Draft Report are both unsupported and inappropriate. We respectfully request the OIG to (1) withdraw the allegations made in the Draft Report, and (2) encourage the HUD Los Angeles Office ("HUD Los Angeles") to help the Owners continue to maintain and preserve these very important affordable housing properties in one of the most needy urban areas in the country.</p> <p>Before addressing the allegations raised in the Draft Report, we believe it is important to discuss the following preliminary issues relating to this Response.</p> <p>A. <u>OIG Denied Owners a Reasonable Opportunity to Address Draft Report's Allegations.</u></p> <p>The OIG's audit of the Projects was begun in January 2005, the auditors completed their on-site review in late June 2005, and the Draft Report was finally sent to the Owners' general partner nearly a year later on January 19, 2006. Despite the fact that the OIG took nearly a full year to produce the Draft Report, your office refused to allow the Owners more than 14 business days to prepare for the exit conference. We made repeated requests to you to extend the date for the exit conference in order to allow the Owners a reasonable period of time to respond</p>
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to the 40+ page Draft Report. As you know, in refusing to grant this reasonable request, you cited nothing other than the OIG's need to complete its final report by March 3, 2006. As explained in my January 30, 2006 correspondence to you:

... I strongly regret that the Office of the Inspector General was unwilling to provide my client with a reasonable period of time to prepare for the exit conference. ... [M]y client is now being provided with only a few weeks to prepare for an exit conference pertaining to a lengthy Draft Report that (1) includes information relating to 6 projects over a 6 year period, (2) relates to an audit that was conducted by HUD over most of last year; (3) includes findings not previously disclosed to my client; and (4) identifies recommendations that, among other things, involve very substantial amounts of money and pertain to tens of thousands of work orders and time sheets. We will, of course, endeavor to make the exit conference a meaningful meeting for both HUD and my client. We hope that you too will work with us to ensure that the final Report is accurate and that my client is given a reasonable opportunity to address this very important matter.

Comment 1

During the exit conference, we asked you to allow my client thirty days – and later reduced to eleven business days – to prepare a response to the Draft Report. Among other things, this time was needed in order for us to review materials (which amounted to over 500 pages of documents) that we requested from the OIG during the exit conference. The additional time was also needed to respond to items, such as the OIG's use of the Saylor cost construction index, that were never previously raised by the OIG in any draft findings – and that, based on the OIG's own calculations, would result in a claim for millions of dollars! Again, you refused this reasonable request – and your justification for such refusal was again based on nothing other than OIG's need to complete its final report by March 3, 2006.

We most certainly respect the OIG's need to complete its work in a timely manner. However, the OIG's concern for expediency – particularly when the OIG took a year to complete the audit – should not permit the OIG to substantially prejudice the rights of an audited party to submit an accurate and complete response to the OIG's allegations. The OIG never provided any explanation as to the apparently arbitrary March 3rd deadline. The OIG's refusal to approve the above-referenced extension requests was both unreasonable and unjustified.

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B. The OIG Ignored the Unique Characteristics of the Projects.

The unique characteristics of the Projects present a number of difficult challenges for the Owners and the Projects' management agent (the "Management Agent"). The Projects are six scattered site properties located just east and south of downtown Los Angeles. This area has a high crime rate, heavy drug and gang activity, and a large homeless population. To further complicate the situation for the Owners and the Management Agent, each of the Projects was constructed in the 1930's and is well over 70 years old. Undertaking repairs to such pre-World War II buildings is far more complicated than those performed on newer buildings. If this situation wasn't difficult enough, add to it the fact that, over the past five years, HUD Los Angeles has consistently refused to grant much-needed rent increases (even though HUD's own personnel indicate that the rents are "extremely low") and replacement reserve account releases (even though the replacement reserve balances are four to five times the minimum balance typically required by HUD for such projects). The OIG's Draft Report makes no mention of these conditions, nor does it reflect the fact that nearly all of the Projects have consistently received passing REAC scores. The omission of these important facts from the Draft Report defies explanation.

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C. The OIG Failed to Recognize Advantages of Central Field Office.

As further discussed below, because the Projects are six scattered site properties, the Owners determined that maintaining six separate offices, one for each Project, was impractical, inefficient and unnecessarily expensive. In response to this situation, the Owners and Management Agent elected to lease a single centralized office that could be used to conduct front-line operations for all of the Projects. The centralized office has permitted the Projects to realize significant economic (and non-economic) benefits.

HUD itself has recognized the advantages of such centralized operations and the need for many properties to have an office to conduct front-line operations. For reasons that remain unclear to us, however, the OIG fails to acknowledge the important role that a centralized field office has played in effectively and efficiently operating these scattered site Projects. The OIG also appears to have given little to no weight to the fact that (1) issues surrounding the centralized field office were previously addressed by the Owners with HUD Los Angeles nearly five years ago; and (2) the Projects' auditor, the Reznick Group, one of the most well-respected audit firms in the country, has previously cleared the prior audit finding identified with respect to the centralized field office.

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D. The Projects' Auditor, the Reznick Group, Carefully Reviewed the Projects' Financial Operations to Ensure Compliance with HUD Requirements.

For the past four fiscal years, the Reznick Group, one of the top public accounting firms in the country, has prepared the financial statements for each of the six Projects. Each year, the Reznick Group performs literally thousands of audits of affordable housing projects. Few, if any, other accounting firms can match the experience of the Reznick Group with respect to HUD accounting and financial requirements. In fact, the Reznick Group has trained some of HUD's own personnel on such requirements. A brief description of the Reznick Group's accounting services is included at Exhibit A. Further information regarding the Reznick Group can be found at www.reznickgroup.com. We are grateful for the Reznick Group's valuable assistance in helping us to address the issues raised in the Draft Report.

As discussed in further detail below, some of the allegations made by the OIG relate to matters that were specifically reviewed by the Reznick Group. The Reznick Group has carefully articulated the reasons why it "cleared" the findings relating to such matters. We respectfully request the OIG to give the Reznick Group's analysis the due consideration it deserves.

Further, for your information, the Owners have also retained the accounting firm of Richard Tremelling (the "Tremelling Firm") to assist in resolving issues relating to the Draft Report. Mr. Tremelling is a CPA that has specialized in accounting matters relating to HUD-regulated projects for over 32 years. He has worked directly with HUD Offices throughout that period, and he has also been retained by HUD to assist HUD Region IX personnel on matters pertaining to financial statements. A brief description of Mr. Tremelling's prior experience is also included at Exhibit A.

E. The OIG Wrongly Recommends Imposition of Civil Money Penalties, Double Damages Remedies and Equity Skimming Action.

According to the recommendations included with Finding 1, the OIG will recommend the imposition of civil money penalties, pursuit of double damages remedies, and pursuit of alleged equity skimming violations. The plain language of the relevant statutes clearly indicates that, even if the Owners/Management Agent had violated HUD requirements, no action would lie under such statutes. The OIG has not provided any evidence indicating that the Owners/Management Agent "willfully" or "knowingly" violated any HUD requirements. In fact, as further discussed below, nearly all of the OIG's allegations relate to matters that: (1) were subject to annual audit by the Reznick Group, (2) were previously addressed directly by the Owners/Management Agent with the HUD Los Angeles, (3) are

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based on HUD "requirements" that don't actually exist, and/or (4) are clearly inconsistent with HUD's published requirements.

F. The Owners Are Prepared to Work Together with the OIG Towards an Amicable Resolution of this Matter.

As the OIG can rightly attest, the Owners and the Management Agent have continually sought to accommodate every request made of them by the OIG's staff. All information requested by the OIG's staff was promptly provided. The Owners/Management Agent provided the OIG's staff with space to conduct the OIG's activities throughout the OIG's lengthy on-site review. Also, we note – somewhat to our own amazement – that the OIG never requested to speak with a supervisor of the Management Agent or a supervisor of Management Agent's identity-of-interest ("IOI") maintenance contractor (the "Maintenance Company"). While it remains unclear to us why the OIG would not want to discuss the findings with such supervisory personnel, we hereby confirm to the OIG that these supervisors are prepared to work with the OIG to resolve the findings.

The Owners also remain ready to work with the OIG to resolve this matter in a manner acceptable to all parties involved. With this in mind, the Owners understand that HUD may seek to have (1) the Owners prepay the loans on the Projects and terminate the related FHA insurance, and (2) the project-based Section 8 assistance terminated (and converted to voucher assistance). Although the Owners have a commitment to providing affordable housing in this area, they are prepared to work with HUD to terminate the FHA insurance and Section 8 subsidy, and facilitate a conversion of the Projects to market-rate housing. If the OIG would like to address these options further, the Owners will gladly participate in such discussions.

RESPONSE TO FINDINGS

Each of the individual findings cited in the Draft Report is discussed below.

FINDING 1: THE PROJECTS PAID \$2,980,984 FOR INELIGIBLE EXPENSES

GENERAL ALLEGATION: In the Draft Report, the OIG alleges that the Projects' Owners and the IOI Management Agent "used \$2,980,984 in project funds for ineligible expenses." The OIG asserts that "[p]ayment of these ineligible costs was a result of the owner/management agent ignoring HUD requirements and a lack of effective procedures and controls."

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GENERAL RESPONSE: As further discussed below, this allegation is false. The Owners and Management Agent did not ignore HUD requirements, nor did they lack effective procedures and controls to ensure that project costs were reasonable. The OIG is wrongly attempting to require the Owners and Management Agent to comply with HUD requirements that do not exist. Thus, in Finding 1, the OIG recommends a demand for the repayment of nearly \$3 million dollars, but fails to cite a single statute, HUD regulation, HUD notice or any specific HUD Handbook provision in support of its position. The OIG's findings are, for the most part, based on blanket references to "the requirements contained in HUD Handbook 4381.5 REV-2" ("Handbook 4381.5 ") without any identification of the specific Handbook provision alleged to have been violated. If the OIG has concluded that the Owners/Management Agents violated HUD requirements, the OIG certainly should be required to identify the specific HUD requirements at issue. This lack of specificity on the part of the OIG, particularly when it is tied to an OIG recommendation to demand the repayment of millions of dollars, is inexcusable.

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To date, the relevant statutes, regulations, notices and handbooks identify relatively few "requirements" relating to the use of IOI contractors. For example, the Project Owner's/Management Agent's Certification, form HUD 9839-B (the "Owner/Agent Certification"), simply indicates that the project owner and management agent must (1) disclose IOI relationships to HUD, (2) ensure that all expenses are reasonable and necessary, and (c) refrain from using IOI contractors unless the cost incurred by the project are "as low as or lower than arms-length, open market purchases." The Owners/Management Agent did not use any IOI contractors unless these threshold requirements were satisfied.

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Each IOI relationship was properly disclosed to HUD on the Owner/Agent Certification. The Draft Report contains no allegations indicating otherwise. The costs incurred by the Owners/Management Agents were reasonable and necessary expenses. The Reznick Group, a nationally recognized accounting firm that is considered one of the foremost experts on HUD accounting practices (and which provides training to HUD on HUD's own requirements), has expressly confirmed through its own bid-testing and other audit procedures that the costs incurred by the Projects were, in fact, "reasonable." And finally, to ensure that all costs incurred were "as low as or lower than arms-length, open market purchases," all services were competitively bid in accordance with the "Contracting Guidelines" set forth in HUD Handbook 4381.5, Section 6.50. Specifically, for the relevant services, the Owners/Management Agent:

1. solicited written cost estimates from at least three contractors for any contract, ongoing supply or service which was expected to exceed \$10,000 per year, or the threshold established by the HUD Area Office with jurisdiction

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over the project (and they solicited verbal or written estimates for those costing less than the above-referenced threshold amount); and

2. retained documentation of all bids as part of the project records for three years following the completion of the work.

We submit that the OIG has failed to satisfy its burden of proving a material violation of the above-referenced HUD requirements by the Owners/Management Agent. Based upon the information contained in this Response, we respectfully request the OIG to delete Finding 1 from the Draft Report.

A. Specific Allegation – Contracting for Maintenance and Accounting on a Noncompetitive Basis: The Draft Report acknowledges that HUD rules expressly permit the use of IOI contractors to provide maintenance and accounting services. The OIG alleges, however, that the Owners and Management Agent contracted on a "noncompetitive basis" and that they did not have "procurement procedures and controls in place to ensure the [IOI] contractors had to compete with outside companies and therefore, keep costs reasonable." According to the OIG, this alleged violation of HUD requirements caused the Projects to be charged \$1,873,059 in excessive maintenance costs and \$365,734 in excessive accounting costs.

Specific Response: As further discussed below, this allegation is false.

I. **Services Were Competitively Bid in Accordance with HUD Contracting Requirements**

The OIG can not legitimately dispute the fact that the Owners/Management Agent contracted for the relevant services on a "competitive basis," per the applicable HUD requirements. The bidding procedures used by the Owners/Management Agent ensured that IOI contractors had to compete with outside contractors to keep costs reasonable. The procurement procedures and controls included, among others, the "Contracting Guidelines" discussed above, as well as other procedures reviewed and approved by the Reznick Group in connection with its preparation of the Projects' financial statements over the past 4 fiscal years.

Over a hundred competitive bids were obtained over the past 5 years in order to ensure that the fees charged to the Projects were "as low as or lower than arms-length, open market purchases." See Owner/Agent Certification, Section 3.d. All such bids were available for the OIG's review during its on-site audit. A sample of such bids was provided to the OIG's staff by Tremelling & Associates (the "Tremelling Firm") on February 1, 2006. A copy of many of the bids is included at Exhibit 1. Although the competitive bids clearly demonstrate the reasonableness of

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the costs incurred by the Projects, the Draft Report contains absolutely no mention of such bids. In fact, the Draft Report appears to ignore the fact that any such competitive bids even exist.

II. Contracting Procedures and Fees Were Properly Subjected to Annual Review by the Reznick Group

Moreover, as mentioned above, the competitive bidding process used by the Management Agent, and the "reasonableness" of the fees charged by the IOI contractors, were reviewed by the Reznick Group in connection with its preparation of the Projects' 2001 year-end financial statements as well as each of the subsequent years' financial statements. Again, the Reznick Group is a nationally-recognized accounting firm that specializes in HUD's accounting requirements. In response to a finding by a predecessor auditor in its year-end 2000 audit report, the Reznick Group reviewed the bidding process employed by the Management Agent. According to the Reznick Group's records, its review was conducted in order to:

... ensure that [the Management Agent] was complying with the competitive bidding rules required for HUD projects ...and to determine that the amounts charged appeared reasonable."
See Exhibit 2.

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The Reznick Group's records indicate that, based upon its review of competitive bids, copies of REAC inspections and follow-up communication, and miscellaneous documentation, "the amounts charged were reasonable" (emphasis added). The Reznick Group further concluded that "any finding or comment relating to excessive charges for maintenance expenses is cleared and is no longer applicable." See Exhibit 2.

In addition to clearing the Finding for fiscal year 2001, the Reznick Group reviewed the reasonableness of the maintenance fees charged, and the relevant procedures, for each of the subsequent fiscal years. None of the subsequent audits raise any findings or provide any other indication that the maintenance charges were somehow unreasonable. Given that the Reznick Group was clearly aware of the issue, and that the firm is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such fees were improper.

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III. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

Per HUD Handbook 4381.5, HUD recognizes the essential role that management reviews play in HUD's monitoring of an owner's and management agent's compliance with HUD requirements. See HUD Handbook 4381.5, § 6.21.b. The Handbook further indicates that, in order to properly monitor projects with a management agent performing certain management functions from a centralized location, HUD should conduct management reviews of such projects "at least once every 18 months." *Id.* at Section 6.33.c. (emphasis added). Regrettably, HUD staff did not comply with its own requirement. Management reviews of the Projects were only completed in 1999 and 2002. No subsequent review, other than the OIG audit, has been conducted since 2002. If HUD has objections to the manner in which the Projects were being operated, it certainly would have been helpful if HUD had not waited six years from the 1999 management review – which happened to reflect a "satisfactory" rating – to notify the Owners/Management Agent of such problems. While the 2002 management reviews reflected an "unsatisfactory rating," the transmittal from the Supervisory Project Manager in the HUD Los Angeles Office clearly explains that: "Most of the deficiencies were due to extremely low rents." See Exhibit 3. Moreover, as further discussed below, due to HUD's consistent refusal to respond to legitimate RR account disbursement requests relating to the Projects, the Projects were often forced to struggle unnecessarily to satisfy HUD requirements. See Exhibit 10 and 17.

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Similarly, as reflected in Exhibit 4, the Projects' Management Agent sent numerous letters to Denise Allison, Project Manager, HUD Los Angeles, back in mid-2001 responding to issues raised by the Projects' auditor relating to the reasonableness of fees charged. See Exhibit 4. The HUD Los Angeles Office never responded to any of these letters. We requested the OIG's staff to provide a copy of any response that HUD may have provided to the above-referenced letters. The OIG's staff confirmed that it did not have information reflecting any responses from HUD. Again, if HUD had an objection to the Owners/Management Agent's practices, it should not have allowed the practices to continue for many years without raising them with the Owners/Management Agent.

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Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

Before addressing the OIG's allegations in Finding 1 further, we would like to comment on a few issues raised by the OIG's staff with respect to this Finding during the exit conference. First, as indicated above, the Owner and Management

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Agent retained the solicited bids for the three-year period specified in Handbook 4381.5 (and, in some instances, such bids were retained for an even a longer period of time). Nevertheless, at the exit conference, the OIG's staff indicated that the bids should have been retained for nearly six years, back to 1999, when the Maintenance Company first began performing services for the Projects. The OIG's staff did not cite any specific HUD provision to support this position – and thus, it's not surprising that no mention of any such requirement is contained in the Draft Report. However, the OIG's staff suggested that since Handbook 4381.5 requires the retention of bids for 3 years after the work is "completed," the OIG concluded that the Maintenance Company's work would not be "completed" until it finished any and all work that was the subject of its contract with the Projects. Of course, if the Maintenance Company continues to perform services to the Projects, and the OIG's interpretation is applied, the Projects could theoretically be forced to retain bids for decades. This position is contrary to HUD's own requirements as well as common sense. We are at a complete loss to understand how competitive bids received in 1999 are somehow necessary to evaluate the reasonableness of fees incurred decades into the future – or, for that matter, even for fees incurred in 2006.

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Second, during the exit conference, the OIG's staff indicated that the Owners and Management Agent were required to obtain bids from other full service contractors that could perform all of the same services (both generalized labor and specialty trades) as the Maintenance Company. Again, the OIG's staff did not cite any specific HUD rule, regulation or issuance to support this position. We note, however, that the Management Agent confirmed that, in the past, it sought to obtain bids from other "full service" maintenance companies. However, it found that many such companies actually subcontracted out the specialty work because they did not keep the specialized laborers on staff. As a result, it was difficult if not impossible to obtain the types of bids suggested by the OIG's staff. Further, since only a few contractors are willing to provide written bids, and even fewer are actively pursuing work in high-crime areas such as south central Los Angeles, it's not surprising that such bids were especially hard to come by.

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Third, the OIG's staff questioned why the issue of the allegedly excessive charges was raised in the year-end 2000 audit report for the Projects prepared by John Awad, CPA, but was "cleared without comment" in the year-end 2001 audit report prepared by the Reznick Group. To our knowledge, there is no HUD or GAAP requirement indicating that the detail relating to "cleared" findings must be included in a project's audit reports. The Reznick Group, like many other accounting firms, often provides the detail relating to such cleared findings in a "Memo To File" or other similar document rather than in the audit report itself. As discussed above, the records prepared by the Reznick Group in connection with its preparation of the year-end 2001 audit report indicates that the bidding process used was proper and "the amounts charged were reasonable."

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B. Specific Allegation – Excessive Labor Rates: In the Draft Report, the OIG alleges that, between January 2000 and June 2005, the Maintenance Company, an IOI contractor, billed the Projects more than \$3.7 million for maintenance and repair services, including more than \$1,763,885 in excessive service costs. The OIG asserts that the Maintenance Company charged labor rates of \$30 to \$55 per hour, depending on the employee performing the work, and it charged \$50 to \$65 for an hour or less of service. The OIG's staff also claims that the difference between the amounts paid to the Maintenance Company's employees and the amounts billed to the Projects was "unreasonably high."

The Draft Report indicates that, for purposes of evaluating the "reasonableness" of the expenses charged, the OIG "compared the amounts [the Maintenance Company] charged ... to the standard rates for open shop (nonunion) general laborers documented in Saylor construction cost indices." Based upon its use of the Saylor construction cost indices, the OIG's staff asserts that the Maintenance Company realized "an excessive profit margin."

Specific Response: As further discussed below, this allegation is false.

I. Compliance with HUD's Published Requirements

The expenses cited as excessive by the OIG were subjected to a competitive bidding process conducted in accordance with HUD's requirements. Per the Management Agent's Handbook, at least three written cost estimates were obtained for contracts expected to exceed the threshold established by the applicable HUD Area Office. The bids were taken for the express purpose of confirming that the costs charged were "as low or lower than arms-length, open-market purchases," as required by HUD (see Owner's/Management Agent's Certification). The bids confirm that, in fact, the expenses charged by the Maintenance Company were reasonable and satisfied HUD's requirements.

II. No Requirement for Compliance with Saylor Index

As indicated above, the OIG does not rely on any statutory provision or any HUD issuance for purposes of concluding that the costs charged by the Maintenance Company were "excessive," or that the contractor realized an "excessive profit margin." Instead, the OIG based its recommendation for repayment of over \$1.7 million on the Saylor construction cost index – an index that is nowhere to be found in the applicable HUD issuances. To our knowledge, HUD has never adopted the Saylor construction cost index as a limitation on expenses charged to HUD-regulated projects. Also, contrary to the OIG's assertion, HUD has not issued any requirements governing permissible profit margins. Instead, the HUD issuances

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correctly focus on whether the costs charged are reasonable and competitive with the open market – *i.e.*, the costs must be "as low or lower than arms-length, open-market purchases" (see Owner's/Management Agent's Certification). The bidding process used by the Management Agent satisfied this requirement.

Even if HUD had properly adopted the Saylor's construction cost index as the standard for establishing the reasonableness of costs charged, Saylor itself indicates that its indices are simply intended to be used for "ballpark" estimating (see www.saylor.com). These "ballpark" figures cannot possibly provide any sort of precise calculation of excess charges incurred by a project. If the federal government seeks to make a claim for repayment of monies, it must establish the amount owed with a reasonable degree of specificity – not "ballpark" guesses.

Further, contrary to the OIG's allegation, the Saylor construction cost indices, if properly applied, do not support the OIG's claim that the expenses incurred were unreasonable. Specifically, the supporting documentation to the Draft Report indicates that the OIG's staff assumed that the vast majority of the 89,000 labor hours in question should be billed at the general laborer rate of \$21.50 per hour, and none of the laborers should be billed at a labor rate in excess of \$32.25 per hour. Saylor itself estimates that laborers providing services such as carpentry, electrical work, painting, drywall or plumbing should be billed at amounts two or three times greater than the general labor rates applied by the OIG. For example, a general carpenter would be billed at \$59.22 per hour, a general painter at \$57.33 per hour, a plumber at \$58.64 per hour, and an electrician at \$68.05 per hour (each subject to adjustment by the city conversion factor).

At the risk of repeating ourselves, we again note that HUD has never adopted the Saylor construction cost index as a limitation on expenses charged to HUD-regulated projects, nor has it issued any requirements governing permissible profit margins. IOI contractors are not prohibited from realizing a profit so long as the costs charged are reasonable and they are "as low or lower than arms-length, open-market purchases."

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As described in further detail on Exhibit 5, many of the Maintenance Company's employees have specialized skills that justify a labor rate well in excess of that of a general laborer. For example, the Maintenance Company's supervisor's resume indicates that he has over 35 years in the construction industry, that he has a general contractors license, and that he has attended various construction management educational programs. The resumes of other Maintenance Company employees identify: (1) an employee who is a licensed locksmith, who also does plumbing, electrical and painting work, and who has worked at the Projects for over 22 years; (2) an employee who works as an electrician, who has a high voltage certification, and who has worked at the Projects for over 22 years; (3) an employee

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who works as an electrician, who has a diploma in residential and commercial electricity, and who also does plumbing, flooring, welding and construction work; (4) an employee who has worked as a landscaper at the Projects for over 16 years; (5) an employee who works as an electrician and is certified as such, and who has worked at the Projects for over 14 years; and (6) an employee who does painting, framing, drywall, foundations, plumbing and electrical work, who spent 11 years working for a construction company doing similar work, and who has worked at the Projects for about 5 years. See Exhibit 5.

Also, California counsel has confirmed that the Maintenance Company has a B-1 general contractors license issued by the State of California that permits the Maintenance Company to render full maintenance services to non-affiliated property owners. The counsel has further confirmed that, under California law, a contractor with a B-1 general contractors license may provide numerous services that would ordinarily require a sub-specialty (*i.e.*, plumbing, electrical). Thus, given that many of the Maintenance Company's personnel are qualified to provide such specialty services, the OIG staff's use of "general labor rates" to estimate allegedly excessive expenses further compounds the problems associated with the OIG staff's improper use of the Saylor indices.

III. Cost Breakdown Further Reflects Reasonableness of Fees

The reasonableness of the charges incurred is also reflected by an analysis of the component parts of the relevant labor rates. Per the Draft Report, the six Projects were charged \$3,701,965 for over 89,000 labor hours, or approximately \$41 per hour, for the services of the Maintenance Company's employees. These fees are clearly reasonable assuming the OIG correctly accounts for the salaries paid to the employees, the various out-of-pocket costs associated with the employment of such employees, and reasonable amounts covering overhead and profit. For example, let's start the analysis with a Maintenance Company employee that earned a salary of \$18 per hour. Based upon information provided by the Reznick Group and the Tremelling Firm, a reasonable estimate of the various out-of-pocket costs associated with such employee – including federal and state payroll taxes (\$2.43 per hour), health benefits (\$1.51 per hour), vacation/sick pay (\$.72 per hour), holiday pay (\$.96 per hour), workers' compensation (\$2.20 per hour), car allowance (\$1.16 per hour), overtime pay (\$1.40 per hour), and related costs – is approximately 60% of the hourly salary, or an aggregate cost of approximately \$28.80 (\$18 X 1.60). Add to that amount a reasonable allowance (35%) for overhead and profit, the aggregate cost is increased to over \$38.30. This number is plainly consistent with the labor costs actually incurred by the Projects.

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IV. Contracting Procedures and Fees Were Properly Subjected to Annual Review by the Reznick Group

As indicated above, the Reznick Group reviewed the reasonableness of the maintenance fees charged, and the relevant procedures, for fiscal year 2001 and each of the subsequent fiscal years. None of these audits raises any findings or provide any other indication that the maintenance charges were somehow unreasonable. Given that the Reznick Group was clearly aware of the issue, and that the firm is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such fees were improper.

V. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

Per HUD Handbook 4381.5, HUD recognizes the essential role that management reviews play in HUD's monitoring of an owner's and management agent's compliance with HUD requirements. See HUD Handbook 4381.5, Section 6.21.b. The Handbook further indicates that, in order to properly monitor projects with a management agent performing certain management functions from a centralized location, HUD should conduct management reviews of such projects "at least once every 18 months." HUD Handbook 4381.5, Section 6.33.c. (emphasis added). Regrettably, HUD staff did not comply with its own requirement. Management reviews of the Projects were only completed in 1999 and 2002. No subsequent review, other than the OIG audit, has been conducted since 2002. If HUD had any objections to the labor rates charged by the Projects, it certainly would have been helpful if HUD had not waited six years from the 1999 management review – which reflected a "satisfactory" rating – to notify the Owners/Management Agent of such problems.

Similarly, as reflected in Exhibit 4, the Projects' Management Agent sent numerous letters to Denise Allison, Project Manager, HUD Los Angeles, back in mid-2001 responding to issues raised by the Projects' auditor relating to the reasonableness of fees charged. See Exhibit 4. The HUD Los Angeles Office never responded to any of these letters. We requested the OIG's staff to provide a copy of any response that HUD may have provided to the above-referenced letters. The OIG's staff confirmed that it did not have information reflecting any responses from HUD. Again, if HUD had an objection to the Owners/Management Agent's practices, it should not have allowed the practices to continue for many years without raising them with the Owners/Management Agent.

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Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

C. Specific Allegation – Improper Charges for Maintenance Company's Supervisor: According to the Draft Report, between January 2000 and September 2001, the Management Agent and the Maintenance Company charged the six Projects an aggregate amount of \$75,674 for payroll costs for the supervisor of the Maintenance Company. The OIG alleges that these charges were not based on specific work performed by the contractor, but were instead allocated as if he were one of the Management Agent's staff performing eligible front-line activities. The OIG asserts that the supervisor's payroll was part of the Maintenance Company's overhead costs, that it was already compensated as part of the maintenance billings, and that it represents an ineligible duplicative charge.

Specific Response: As further discussed below, this allegation is false. Contrary to the allegation made by the OIG, the costs at issue were, in fact, based on specific work performed by the Maintenance Company's supervisor on front-line activities. The services included, among others, coordinating and attending various inspections at the Projects including Los Angeles City inspections, Los Angeles County Health inspections, HUD/REAC inspections, fire/liability insurance underwriting inspections, mortgage lender inspections and the owner's annual inspection. In addition, the Maintenance Company supervisor was often required to conduct pre-inspections prior to inspections conducted by government agencies, and post-inspections following the completion of required repair work. Also, as part of the post-inspection process, any inspection report issued must be studied and in many cases a written response must be prepared. All of the foregoing are front-line expenses that are necessary activities in "maintaining the project." See HUD Handbook 4381.5, Section 6.38a.(1).

A sample of documentation reflecting the reviews/inspections performed by the Maintenance Company's supervisor is included at Exhibit 6. Because these inspections were conducted four or more years ago, the Projects no longer retain a complete set of such documents.

Although the issue is not addressed by the OIG, we note that if the above-referenced services were not performed by the Maintenance Company's supervisor, the Projects most certainly would have been forced to pay someone else to perform such front-line functions. The Projects were not, therefore, harmed as a result of the Maintenance Company performing such services.

The OIG appears to assume that HUD Handbook 4381.5 prohibits the supervisor of a contractor to a management agent from performing front-line services. Handbook 4381.5 identifies limitations relating to the performance of

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front-line functions by the management agent's supervisor. By its plain language, however, these limitations do not extend to a contractor of the management agent. See HUD Handbook 4381.5, Section 6.39.

II. Contracting Procedures and Fees Were Properly Subjected to Annual Review by the Reznick Group

As noted by the OIG, the auditor for the Projects for fiscal year 2000, Mr. Awad, questioned the salary of the Maintenance Company's supervisor as a front-line expense. Questions were raised at the time as to whether Mr. Awad understood the distinction between the functions of the Management Agent and those of the Maintenance Company. As indicated above, for fiscal year 2001, the Reznick Group was engaged as the Projects' audit firm. The Reznick Group cleared Mr. Awad's finding. The Reznick Group has continued as the Projects' audit firm through the present. Throughout this entire period, the Reznick Group has not identified any findings of improper accounting or financial management relating to the compensation paid to the Maintenance Company's supervisor for the performance of front-line functions. Given that the Reznick Group was clearly aware of the issue, and that the firm is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such fees were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

D. Specific Allegation – Improper Inspection Charges: The Draft Report states that the Maintenance Company charged the six Projects an aggregate amount of \$33,500 for inspections conducted between May 2003 and May 2005. According to the OIG, the invoices were supposed to compensate the contractor for unit inspections performed by the maintenance supervisor, but the costs were not based on actual work performed. The OIG indicates that the Maintenance Company charged the same amount to each Project on consecutive invoices, an apparent allocation of the maintenance supervisor's payroll.

Specific Response: As further discussed below, this allegation is false. The maintenance supervisor coordinated and attended a number of different types of inspections including Los Angeles City inspections, Los Angeles County Health inspections, HUD/REAC inspections, fire/liability insurance underwriting inspections, mortgage lender inspections and the owner's annual inspection. In addition, the supervisor was often required to conduct pre-inspections prior to inspections conducted by government agencies, and post-inspections following the completion of required repair work. Also, as part of the post-inspection process, any inspection report issued must be studied and in many cases a written response

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must be prepared. A sample of documentation reflecting the reviews/inspections performed by the Maintenance Company's supervisor is included at Exhibit 7. Each of the foregoing are front-line expenses that are necessary activities in "maintaining the project." See HUD Handbook 4381.5, Section 6.38a.(1).

For the above-referenced services, the Projects were billed five hours at the rate of \$50 per hour, twice a month. While the total billing for the six projects is 60 hours per month (5 hours X 2 times per month X 6 projects), the Management Agent has confirmed that the time actually spent providing these services is significantly greater than 60 hours per month. Although the OIG's staff may dispute the allocation of these costs among the Projects, it is clear that costs relate to the performance of legitimate front-line services.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

E. Specific Allegation – Marked Up Maintenance Costs: According to the Draft Report, the Maintenance Company marked up costs by up to 35% when it purchased materials or used another contractor to perform repairs. The Draft Report states that the HUD regulatory agreements and HUD Handbook 4381.5 prohibit the owner and management agent from adding surcharges to actual costs.

Specific Response: As further discussed below, this allegation is false.

I. **Services and Goods Were Competitively Bid in Accordance with HUD Contracting Requirements**

The Owners/Management Agent contracted for the relevant services and goods on a "competitive basis," per the applicable HUD requirements. The bidding procedures used by the Owners/Management Agent ensured that IOI contractors had to compete with outside contractors to keep costs reasonable. The procurement procedures and controls included, among others, the "Contracting Guidelines" discussed above, as well as other procedures reviewed and approved by the Reznick Group in connection with its preparation of the Projects' financial statements over the past 4 fiscal years.

Over a hundred competitive bids were obtained over the past 5 years in order to ensure that the fees charged to the Projects were "as low as or lower than arms-length, open market purchases." See Owner/Agent Certification, Section 3.d. All such bids were available for the OIG's review during its on-site audit. Also, a sample of such bids was provided to the OIG's staff by Tremelling & Associates (the "Tremelling Firm") on February 1, 2006. A copy of many of the bids is included at Exhibit 1. Although the competitive bids clearly demonstrate the reasonableness of

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the costs incurred by the Projects, the Draft Report contains absolutely no mention of such bids. In fact, the Draft Report appears to ignore the fact that any such competitive bids even exist.

II. The Additional Costs were Proper

The Management Agent has confirmed that the additional charges cited by the OIG were intended to cover legitimate costs including the following: labor spent in examining, purchasing, collecting, transporting, loading and unloading materials and storage of materials purchased in volume. The additional charges were only applied to materials purchased in volume, thereby resulting in overall discounts to the Projects.

The information provided indicates that the additional charges imposed on services related to a short period of time in 2001 when the Management Agent charged an additional amount for services related to landscaping/grounds keeping services then performed by third party contractors. These additional charges were intended to cover certain front-line costs relating to additional oversight and potential increased insurance risks. While the OIG does not allocate a dollar amount to these charges, the information provided indicates that the additional charges for such services is probably less than \$10,000 in the aggregate.

III. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

The Management Agent was questioned about the additional charges following the submission of the Projects' year-end 2000 audit reports. By letter dated June 11, 2001 from the Management Agent to Denise Allison of HUD's Los Angeles Area Office, the Management Agent explained that: "\$35.00 is a competitive rate and less than all bids received, materials are marked up 33% when purchased wholesale." See Exhibit 8. The Management Agent indicates that, with the exception of the OIG's current audit, the issue of the additional costs was never raised by HUD again. We requested the OIG's staff to provide a copy of any response it may have provided to the above-referenced June 11, 2001 letter relating to the additional costs. The OIG's staff confirmed that it did not have a copy of any HUD response to the June 11, 2001 letter.

If HUD had objections to the additional charges, it most certainly should not have waited over 4 years to raise the issue in an OIG audit report. Although the Management Agent never received a response to its correspondence, the Management Agent has confirmed that the practice of imposing such additional charges was discontinued at or about the time of the June 11, 2001 letter. It is our

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understanding that the practice was discontinued in order to eliminate even any appearance of impropriety with respect to the Projects.

IV. Contracting Procedures and Fees Were Properly Subjected to Annual Review by the Reznick Group

As indicated above, the Management Agent was questioned about the additional charges following the submission of the Projects' year-end 2000 audit reports. The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the additional charges imposed by the Management Agent. Given that the Reznick Group was clearly aware of the issue, and that the firm is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

F. Specific Allegation: According to the Draft Report, the maintenance work performed on a sample of 60 units showed work order repairs performed "since 2003" were "questionable." The OIG cited alleged examples of work that was of "inadequate" quality, incomplete work and other "questionable work."

Specific Response: As further discussed below, this allegation is false.

I. OIG Has Ignored Factors Affecting Maintenance of 70+ Year-Old Affordable Housing Projects in Urban Areas

There are few, if any, 70+ year-old affordable housing projects in urban areas like south central Los Angeles that don't have physical condition deficiencies and some deferred maintenance. These conditions are often exacerbated by tenant neglect and abuse of their units and vandalism. The OIG apparently ignored these factors for purposes of its inspection of the Projects' units and common areas.

Moreover, given that many of the deficiencies cited by the OIG relate to repairs completed a number of years ago, it is extremely difficult to understand how the OIG can now argue that these repairs were somehow "inadequate," "incomplete" or "questionable." Notwithstanding the foregoing, we have attempted to address each of the cited deficiencies in detail at Exhibit 9.

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II. OIG Has Failed to Recognize the Impact on Project Maintenance of HUD's Refusal to Approve Legitimate RR Account Releases

The OIG has failed to recognize the fact that the Owners and Management Agent have done a relatively commendable job maintaining the Projects. Regrettably, the Owners/Management Agent's efforts to properly maintain the Projects has been frustrated over the past five years due to the local HUD Office's consistent refusal to approve legitimate requests for much-needed replacement reserve ("RR") account releases and rent increases. In fact, based upon the information provided, the local HUD Office did not even respond to most such requests for RR account releases or rent increases. A sample of such requests is included at Exhibit 10.

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The local HUD Office's refusal to approve RR account releases is particularly difficult to understand given that the accounts contained a substantial amount of extra funds. The Projects' RR accounts currently hold approximately \$4,500 per unit – or 4.5 times the \$1,000 minimum balance typically required by HUD on such projects. When the Management Agent first began managing the Projects back in 1999, the Projects' RR accounts held only about \$500 per unit. If HUD would have simply approved the requested RR releases, most if not all of the deferred maintenance issues could have been fully addressed by now.

III. OIG Has Failed to Recognize the Difficulty of Maintaining Projects Restricted by "Extremely Low Rents"

As reflected by correspondence from HUD's own personnel, the Projects have long struggled due to low rental rates imposed by HUD. For example, in connection with the "unsatisfactory" management review rating received by the Projects in 2002, Ms. Yvonne Stevens, Supervisory Project Manager, HUD Los Angeles, explained that "[m]ost of the deficiencies were due to extremely low rents." See Exhibit 3. The management review further indicated that rents were "way below average." We find it particularly discouraging that the OIG now raises issues relating to the physical condition of the Projects that could (and should) have been properly addressed by HUD years ago. To our knowledge, HUD has yet to provide any meaningful explanation as to why it routinely refused to approve legitimate rent increase requests.

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IV. OIG Has Failed to Recognize the Overall Commendable Condition of the Projects Given the Above-Referenced Circumstances

Finally, we note that the physical inspection scores for the Projects indicate that, despite the local HUD Office's unwillingness to approve RR account releases and/or rent increases, the Owners and Management Agent have continued to strive

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to maintain the Projects as required by HUD. In fact, with the exception of Holiday 101B, the most recent physical inspection reports for each of the Projects reflects a passing score (Holiday 101B missed a passing score by only one point out of 100). A few additional examples of the physical inspection scores for the Projects received over the past few years is provided below:

- 75c (Holiday 101A in 2002)
- 74c (Holiday 101A in 2003)
- 70c (Holiday 101A in 2004)
- 93b (Holiday 101B in 2001)
- 78c (Holiday 101B in 2004)
- 84c (Holiday 101C in 2001)
- 93c (Holiday 101C in 2003)
- 84c (Holiday 102 in 2001)
- 84b (Holiday 102 in 2003)
- 71c (Two Worlds II in 2001)
- 91c (Two Worlds II in 2002)
- 75c (LA Pro 30 in 2001)
- 76c (LA Pro 30 in 2002)
- 89c (LA Pro 30 in 2003)

Regrettably, it is only within the past year, when the impact of HUD's denials of RR releases and rent increases has become particularly acute, that the Projects have struggled somewhat to achieve a passing physical inspection score.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

G. Specific Allegation – Improper Charges for Accounting Services:

According to the Draft Report, the Owner and Management Agent contracted with two IOI contractors, Action Bookkeeping and Accounting Data Systems, to provide accounting services for the Projects. The Draft Report indicates that (1) HUD has established a maximum allowable fee for these services of \$7.50 per unit per month, and (2) the \$366,474 in fees the Projects paid the IOI accounting firms from December 2000 through November 2004 exceeded this cap by \$144,714.

In addition, the Draft Report states that, during the period from August 2001 through November 2004, the Management Agent charged the Projects \$221,019 for the direct time of two of its staff providing accounting services to the Projects. The Draft Report further states that, by charging for services through a vendor and then again directly, the Management Agent double charged the Projects for accounting services.

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Specific Response: As further discussed below, this allegation is false.

I. OIG is Relying on Stale and/or Inapplicable Memos Regarding Allowable Fees

In response to the alleged limit on the per unit cost of accounting fees, we asked the OIG's staff to provide us with a copy of "any and all" HUD issuances that impose such limits. In response, the OIG's staff provided us with two items. The first item, a Memorandum to Multifamily Owners and Agents, Los Angeles Multifamily HUD Jurisdiction, dated May 2, 2001, indicates that some 5 years ago HUD identified \$7.50 as "a middle ground charge" for bookkeeping. See Exhibit 11. The second item, a Memorandum to Multifamily Owners and Agents, San Francisco Office Jurisdiction Only, dated June 10, 2003, indicates by its express terms that it "applies to the San Francisco office jurisdiction only." See Exhibit 11.

As indicated above, the OIG is basing its allegation on one 5-year-old memo, and a second memo that does not even apply to the jurisdiction in which the Projects are located. Neither of the memos were issued in the form of any regulation, handbook provision or formal directive. Instead, the memos appear to have been sent as part of some mass mailing by HUD to "Multifamily Owners and Agents" that was to be "effective upon receipt." See Exhibit 11. The Owners and Management Agent have confirmed that, to their knowledge, they never previously received a copy of either of the memos.

Given the foregoing, we respectfully request the OIG to identify to us the legal basis for recommending a demand for repayment based on the above-referenced memos. We believe that such a response from the OIG is warranted since, among other things, we understand that many other owners and management agents in the relevant area never received such memos from HUD.

II. OIG is Wrongly Assuming All of the Fees Charged Pertain to Bookkeeping

We are unable to determine how the OIG computed its estimate of ineligible bookkeeping costs. We respectfully request the OIG to provide supporting documentation reflecting the OIG's computations.

Also, we submit that the OIG's allegation fails to acknowledge that the IOI contractors referenced in the allegation, as well as the two Management Agent personnel cited by the OIG, provide additional services other than bookkeeping. Specifically, among other things, the subject personnel spend substantial portions of their time performing non-bookkeeping functions such as certifying and recertifying tenants. Due to the time constraints imposed by the OIG for submission of this

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response, the Owners/Management Agent have not had an opportunity to prepare the supporting documentation reflecting the allocation of such fees between bookkeeping and non-bookkeeping services. The Owners/Management Agent respectfully request OIG approval for additional time to submit such documentation to the OIG.

III. The Bookkeeping Services Were Competitively Bid in Accordance with HUD Requirements

The Owners/Management Agent contracted for the relevant bookkeeping services on a "competitive basis," per the applicable HUD requirements. A sample of the relevant bids is included at Exhibit 12. As reflected by the sample, the bids obtained were in the amount of \$30 per hour or more. Although HUD may prefer billing on a per unit per month ("pupm") basis, many bookkeeping firms bill on an hourly basis rather than a pupm basis.

The bidding procedures used by the Owners/Management Agent ensured that IOI contractors had to compete with outside contractors to keep costs reasonable. The procurement procedures and controls included, among others, the "Contracting Guidelines" discussed above, as well as other procedures reviewed and approved by the Reznick Group in connection with its preparation of the Projects' financial statements over the past 4 fiscal years.

Based upon the information provided, the bookkeeping services were billed at a rate of approximately \$10.61 per hour, on average. This amount was computed by dividing the total accounting costs included in Item 6351 of the financial statements by 634 (the number of units in the Projects), and then divided again by 12 (the number of months in a year). This rate is clearly competitive with the rates charged by third-party contractors. However, as noted above, we recognize that it is necessary to provide an allocation of the bookkeeping costs included in Items 6310 and 6351 of the financial statements to obtain a truly accurate figure for such costs.

IV. HUD Permits Charges of Actual Bookkeeping Costs.

The information above clearly indicates that the bookkeeping services charged to the Projects were provided at a competitive rate and charged at actual cost. Both the Reznick Group and the Tremelling Firm have confirmed that HUD issuances do not prohibit an owner/agent from charging the actual costs charged by a contractor for such bookkeeping services – even if they exceed \$7.50 pupm – so long as they are otherwise reasonable. Moreover, HUD Handbook 4381.5 expressly indicates that the cost of bookkeeping services for a project performed as part of a centralized bookkeeping system "are treated as a project cost" and "are paid out of

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project funds based on actual costs attributable to the project." See HUD Handbook 4381.5, Section 3.7.c.

V. HUD Permits Upward Adjustments of Allowable Fees for Scattered Site Projects.

HUD permits "add-ons" to allowable fee schedules to address certain unique project features such as scattered site properties. See, e.g., HUD Handbook 4381.5, Section 3.7, Figure 3-4. The Tremelling Firm has confirmed to us that HUD Field Offices have permitted upward adjustments to allowable bookkeeping fees for scattered site properties such as the Projects.

VI. Bookkeeping Fees Were Properly Subjected to Annual Review by the Reznick Group

The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the bookkeeping fees charged to the Projects. Given that the Reznick Group is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

H. Specific Allegation – Improper Charges for Management Agent's President: According to the Draft Report, the Management Agent inappropriately charged the Projects \$380,670 in payroll costs for its President. The payroll costs charged to the Projects ranged from 60 to 70 percent of the President's total salary. The Draft Report indicates that the President was performing "supervisory functions" and that the charges for such services are considered management agent costs and are not eligible for payment from project funds.

Specific Response: As further discussed below, this allegation is false.

I. "President" Functioned as Resident Manager/Superintendent

The OIG correctly notes that HUD Handbook 4381.5 imposes certain limitations on a management agent's ability to charge salaries of the agent's supervisory personnel to a project's operating account. However, the OIG fails to properly recognize the unique features of the properties and wrongly concludes that the "President" was a "supervisor." Standing alone, a title does not establish the

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scope of authority, duty or responsibility of the individual. Thus, with respect to the Projects, the "President" functions more as a traditional "resident manager" or "superintendent" of the six scattered site Projects. The vast majority of his work involves interfacing with tenants; handling tenant problems; coordinating repairs and replacements; approving move-ins; inspecting the units, common areas and building exteriors; pursuing tenant fraud and coordinating evictions. See, for example, Exhibit 13. These are all front-line activities that are typically associated with a resident manager/ superintendent.

Given that the properties are scattered site, and they include over 1,250 residents living in 634 units, the President's role as a resident manager/superintendent is particularly critical to the ongoing operation and maintenance of the Projects. The HUD Handbooks expressly recognize, among other things, that salaries paid to a resident manager or superintendent are allowable project expenses. See Industry User Guide for the Financial Assessment Subsystems – Multifamily Housing (October 15, 2004), Item 6330.

Like most resident managers/superintendents, the President performs some limited oversight functions. Performance of these functions does not, however, cause this individual to become a "supervisor." In fact, just as an example, we note that a supervisor traditionally has check-signing authority with respect to a project's operating account. The Management Agent's President, like most resident managers/superintendents, has no such authority.

Of course, the Projects do have a "supervisor" as that term is used in Handbook 4381.5. The Chief Executive Officer (the "CEO") for the Management Agent, is responsible for providing oversight and supervision with respect to the Projects. Among other things, the CEO reviews the performance of the Management Agent's personnel; assists the Management Agent's personnel with the formation, amendment and implementation of significant policies of the Management Agent; conducts periodic review of applicable financial statements and significant correspondence; and executes bank checks and account withdrawals. Because the CEO is a supervisor, the CEO 's compensation is paid out of the management fee, not from project funds. The Management Agent also has a Chairman that serves as a supervisor. Like the CEO, the Chairman's compensation is paid out of the management fee, and not from the Project's operating account.

The OIG seems to believe that the title of "President," connotes someone in a "supervisory" position. However, the OIG's staff fails to recognize that the Management Agent is a limited liability company, not a corporation, and it does not have traditional officers such as President. The "President" title is used simply because, in many instances, tenants seek to raise their issues/concerns with a senior person such as a "President." It was impractical for the CEO or the Chairman to

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handle all such tenant issues at the six Projects. Therefore, a "President" was designated to serve as an intermediary (or buffer) between the tenants and the supervisors.

In retrospect, perhaps the President should have been formally designated a "resident manager/superintendent." Nonetheless, the title given to this individual does not change the fact that he was properly performing front-line functions and such services were properly chargeable to the Projects as front-line costs.

II. The Projects Don't Have Any Other Personnel Serving as Resident Manager/Superintendent

The Projects don't have any person, other than the "President," earning a salary that is commensurate with the services required of a resident manager/superintendent. The Projects have a number of resident "keyholders" – tenants at the Projects who are responsible for, among other things, assisting with (a) the delivery of tenant complaints to management, (b) the notification to management of adverse conditions, and (c) the collection of rents. None of these keyholders perform services akin to those traditionally required of a resident manager/superintendent. Only the President provides such services.

III. Many of the President's Services are Front Line Costs

The services provided by the President in his capacity as resident manager/superintendent are front-line costs. If the President did not provide these services, the Projects would be forced to pay someone else to do them. The costs of these front-line functions were paid from the Projects' operating account in accordance with its proportionate share of the overall sixty to seventy percent. Compensation for the remaining thirty to forty percent of time was spent performing non front-line functions – and was paid from the management fee.

IV. All Expenses Were Properly Subjected to Annual Review by the Reznick Group

The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the fees charged to the Projects with respect to the President's front-line services. Given that the Reznick Group is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

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Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

I. Specific Allegation – Improper Rent Charges for Central Office: The Draft Report states that the Management Agent charged the Projects \$209,441 for the rental of the Management Agent's central office between 2000 and 2004. According to the Draft Report, not only were these charges ineligible project costs, the charges did not represent an appropriate allocation of the Management Agent's actual costs and covered the cost of the general partner's offices.

Specific Response: As further discussed below, this allegation is false.

I. HUD Expressly Permits Charges for a Project Office

Reasonable expenses incurred by the Projects for front-line management activities include office expenses associated therewith. HUD's rules recognize that the Projects are permitted to establish a project office as part of the Projects' management cost. The expense for such an office may be properly charged to the Projects' operating account as an administrative expense. See Industry User Guide for the Financial Assessment Subsystems – Multifamily Housing (October 15, 2004), Item 6312

II. The Centralized Field Office Provides Important Benefits to the Projects

Because the Projects are comprised of six scattered site properties, a single office at each of the six Projects (or off site) was deemed financially impractical. The past few years have shown that the centralized field office is critical to the proper operation and management of the Projects. Prior to May 2000, the Projects did not have a centralized field office. Lacking such a facility, it was determined that the Projects were unable to operate most efficiently and economically. In order to remedy this situation, in May 2000 the Owners leased office space from the Management Agent. This space is contained within the ground floor of the real property located at 2510 West 7th Street in Los Angeles, California.

Under the terms of the commercial lease signed by the parties, a suite of offices was constructed on the demised premises to suit the Projects' requirements for a field office. A copy of the lease was provided to the OIG during its on-site review. The lease enabled the Projects to acquire a leasehold estate in land specifically described and designed within the ground floor of the 2510 West 7th Street property.

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The leasehold estate granted to the Projects is improved with a suite of interconnected offices including a conference room, reception area, file room and open workspace (collectively, the "Field Office"). By the specific description of the Field Office in the lease and the intention of the parties, the Field Office exists separate and apart from all remaining space on the ground floor (the Projects' historical records are stored in a separate area of the building for which no additional charge is made). The Projects have no other office from which front-line functions are performed.

The space remaining on the ground floor of the 2510 West 7th Street property is the separate leasehold property of the Management Agent. From this separate facility, the Management Agent and its affiliates perform bookkeeping and maintenance functions in addition to other activities not chargeable to the Projects as front-line costs. The Project's Field Office, located on the ground floor of the 2510 West 7th Street property is, therefore, clearly separate and distinct from the Management Agent's office.

As indicated above, the economic benefits associated with the Field Office should be obvious. It is not economically practical for each of the six Projects to devote one of its rental units to front-line office use. Nor would it be practical to staff a single office for each of the Projects. Such an undertaking would result in front-line costs to the Projects far in excess of their current share of all front-line expenses, including rent, in the operation of the single Field Office.

Moreover, the utilization of the Field Office benefits the project by improving the efficiency of the front-line staff. Historical records as well as current bookkeeping records are near at hand. Oversight of the front-line staff is swiftly and more effectively accomplished. The Field Office is centrally located in a business district and easily reached by the Projects' residents.

III. Rent Charged Was a Reasonable and Necessary Expense

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Contrary to the position stated in the Draft Report, the rent for the centralized field office was a necessary and reasonable expense properly charged to the Projects. As discussed above, HUD issuances expressly recognize that the costs related to a "project office" are properly chargeable to a project. See Industry User Guide for the Financial Assessment Subsystems – Multifamily Housing (October 15, 2004), Item 6312.

The rent charged to the Projects for the Field Office was unquestionably reasonable. The information provided indicates that the total monthly rent charged is about \$0.76 per square foot. When the capital improvements (as further discussed below) are added and spread over the five year life of the Lease, the total

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monthly cost is about \$1.22 per square foot, which is apportioned among the six projects according to the number of units owned by each.

The information provided further indicates that, in arriving at the amount of the agreed rent for the Field Office, a survey was conducted of fair market rents charged in the area for comparable space. We have been advised that, in 2000, the charge of monthly Field Office rent at \$1.22 per square foot was, and is today, well below the fair market rent for comparable space. The rental rate charged the Projects for its Field Office is a reasonable rent considering the location and activities conducted thereon.

IV. The Field Office Rent Expenses Were Properly Subjected to Annual Review by the Reznick Group

The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. As further discussed below, a question was raised by the predecessor auditor in 2000 relating to certain capital improvements to the Field Office. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the field office rental fees charged to the Project. Given that the Reznick Group was clearly aware of the central field office rental expense, and that it is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such rental charges were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

J. Specific Allegation – Improper Capital Improvement Charges for Central Office: The Draft Report states that the Management Agent charged the Projects \$140,880 for capital improvements made to the Management Agent's central field office between April, 2000 and January, 2001. According to the Draft Report, the office was not owned by the Projects and any costs related to the office space are overhead expenses that must be paid out of the Management Agent's Fee.

Specific Response: As further discussed, below, this allegation is false.

I. The Central Field Office is owned by the Projects

As discussed above, the Field Office exists separate and apart from all remaining space on the ground floor of the building in which it is located. The OIG was provided with a copy of the related lease. The Field Office leasehold estate is exclusively owned by the six Projects. The fact that the space is leased rather than

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owned in fee simple does not negate the fact that the Projects hold a leasehold interest in the Field Office and its improvements.

II. The Field Office Capital Improvements Were Properly Subjected to Annual Review by the Reznick Group

A finding relating to the capital improvements made to the Field Office was included in the fiscal year 2000 financial audit report for the Projects prepared by John Awad CPA. Questions have been raised as to whether Mr. Awad properly understood that a leasehold estate in land could properly be capitalized for accounting and tax purposes in substantially the same fashion as improvements to a fee simple estate in land. For the fiscal year 2001, the Reznick Group was engaged as the Projects' audit firm. In that year the Reznick Group cleared the finding made in Mr. Awad's audit report for the Projects. In the Reznick Group's records, the firm explained that: "[c]harges associated with front-line activities at the [centralized field office] are substituted for costs that could be charged if each [of the Projects] had an on-site office space to conduct the business of the [Project]." See Exhibit 14. The Reznick Group concluded by stating:

Based upon a reading of HUD Handbook 4381.5 REV-2, Chapter 6, we believe it is reasonable for the client to allocate these offsite capital improvement charges to [the Projects] and will clear the finding when preparing our 2001 audit reports.
See Exhibit 14.

The Reznick Group also prepared the audits for the Projects for each fiscal year subsequent to the 2001 audit. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the field office capital improvements charged to the Project. Given that the Reznick Group was clearly aware of the central field office capital improvements, and that it is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

III. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

In response to questions raised in connection with the 2000 audit of the Projects, the Management Agent sent a number of letters, dated May 25, 2001 and June 11, 2001, to Denise Allison of HUD's Los Angeles Area Office. In the letters, the Management Agent explained that: "The project expenses for the central office costs were tenant improvements for the field office of the scattered sites." See

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Exhibit 4. In the letters, the Management Agent also explained that the auditor for 2000, Mr. Awad, "had never heard of leasehold or tenant improvements." Id. The Management Agent confirmed that, with the exception of the OIG's review during 2005, the issue of the capital improvements was never raised by HUD again. We requested the OIG's staff to provide a copy of any response it may have provided to the above-referenced letters relating to the capital improvements. The OIG's staff confirmed that it did not have a copy of any HUD response to the letters. If HUD had objections to the charges for capital improvements, it most certainly should not have waited nearly 5 years to raise the issue in an OIG audit report

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

K. Specific Allegation – Holiday Apartments Paid Owner's Expenses:

According to the Draft Report, between 2001 and 2004, Holiday Apartments paid \$21,600 in eligible ownership franchise taxes. The OIG asserts that these taxes were the responsibility of the individual partners of the ownership entities and should not have been paid from project funds. The OIG indicates that review of the Projects' general ledgers and related support showed that the Management Agent returned \$10,400 of the ineligible expense payments to the Projects, but \$11,200 had not been reimbursed to the Projects.

Specific Response: The Management Agent has confirmed that, to its knowledge, all of the allegedly ineligible franchise taxes have been returned to the Projects. The Management Agent acknowledges that it made an inadvertent error paying such amounts from project funds. The Management Agent is prepared to provide all necessary assurances that this error will not occur again.

The OIG asserts that an additional \$11,200 in allegedly ineligible franchise taxes must be reimbursed to the Projects. The detail provided by the OIG does not identify which entities that allegedly ineligible tax payments relate to. Before addressing this issue further, we respectfully request the OIG to provide such necessary information.

L. Specific Allegation – Projects Continue to Pay for Similar Ineligible

Expenses: Per the Draft Report, the maintenance, accounting, management office rent and inspection costs were ongoing issues, extending beyond the period of the OIG's review. The OIG indicates that "we anticipate" these issues resulted in additional ineligible charges to the Projects. The OIG further indicates that "we estimate" that after our audit period, through December 2005, the Projects would have been charged \$494,979 in additional ineligible costs including \$301,720 for one year of maintenance, \$100,374 for one year of bookkeeping, \$76,135 for one year of rent, and \$16,750 for six months of inspection costs.

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Specific Response: As further discussed below, this allegation is false. The OIG has the burden of proving that the costs incurred were ineligible. The responses above clearly reflect the fact that the OIG has failed to satisfy this burden. Among other things, the OIG has not yet demonstrated that the Owners/Management Agent violated applicable HUD requirements. Moreover, the information provided to the OIG clearly indicates that the services and goods provided to the Projects were competitively bid and properly documented, and that the costs charged were "as low as or lower than arms-length, open market purchases."

Further, in addition to the OIG's failure to prove that ineligible expenses were incurred, the OIG now seeks to use another "ballpark" estimate as the basis for recommending a demand for repayment. The OIG fails to indicate the likelihood that this ballpark estimate, even if based on legitimate findings, may over-state (or under-state) the potential demand for repayment.

Finally, as indicated above, the Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the charges cited in this allegation.¹ Given that the Reznick Group was clearly aware of such expenses charged to the Projects, and that it is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

FINDING 2: THE PROJECTS WERE NOT MAINTAINED IN GOOD REPAIR AND FREE OF HEALTH AND SAFETY VIOLATIONS

A. Specific Allegation – Project Units Were not Decent, Safe and Sanitary: According to the Draft Report, the OIG conducted a statistical sample of 60 units and identified 166 24-hour health and safety violations, 14 10-day violations and 60 30-day violations. The OIG claims that the violations resulted in 100 percent of the buildings and 83 percent of the units reviewed failing HUD's housing quality standards. A chart identifying the alleged violations was included in the Draft Report. Furthermore, in support of this allegation, the OIG cites:

¹ We note, however, that the Reznick Group did not specifically address the issue of the inspection charges in its audits.

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1. Two Worlds II, 1288 Kingsley, unit C06: Cracked Stove
2. LA Pro 30, 817 Parkview, unit D106: Tub wall separating and deteriorating.
3. Two Worlds II, 420 Union: Detached handrail in common area.
4. Holiday 101-B, 106 Commonwealth: Furnace exhaust not ventilating to exterior of building.
5. Holiday 101-A, 1107 West 42nd Street: Damaged roof access door.

Specific Response: As further discussed in Finding 1 above, the Owners/Management Agent have done a commendable job maintaining the Projects given, among other things: (1) HUD's refusal to grant much-needed RR account releases and rent increases; (2) HUD's own acknowledgement that "[m]ost of the deficiencies [in the Project's condition] were due to extremely low rents;" and (3) that the Projects are over 70 years-old and located in a very high-crime area in Los Angeles with a large homeless population. Also, as discussed in Finding 1 above, the REAC inspections for the Projects confirm the quality of the maintenance of the Projects in past years – and the Projects' unfortunate struggle to address ongoing project needs most recently due to the lack of available cashflow.

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In response to the chart of violations cited by the OIG in this allegation, we note that the OIG is applying a more stringent standard with respect to 24-hour, 10-day and 30-day violations than that imposed by REAC. During the exit conference, the OIG staff admitted that they were not following the REAC protocol. We respectfully request the OIG to identify which HUD rules, if any, it has used to cite such violations. If the OIG intends to apply its own rules, such rules should most certainly be provided to the audited party – and the auditor should be required to justify its reasoning for abandoning the REAC protocol on such matters.

In response to the specific unit deficiencies cited by the OIG as examples of poor maintenance, the Management Agent has confirmed the following:

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1. Two Worlds II, 1288 Kingsley, unit C06: There was no evidence that the "cracked stove" was inoperable or a safety hazard. The crack was covered with aluminum foil for aesthetic reasons. The OIG apparently removed the aluminum foil. The stove has now been replaced.
2. LA Pro 30, 817 Parkview, unit D106: The tub wall separating/deteriorating did not cause the tub to be inoperable, nor did it pose a safety hazard. This was a deferred maintenance item that was sought to be addressed through a mid-term rent increase which identified these problems. As discussed above, the requests were denied or ignored by HUD.

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3. Two Worlds II, 420 Union: The detached handrail in the common the area was likely due to vandalism. The "keyholder" for the building reports that the handrail was properly affixed to the wall earlier in the day.

4. Holiday 101-B, 106 Commonwealth: Based upon the information provided, the furnace exhaust not ventilating to exterior of building may be due to a homeless person trying to re-direct heat. The Projects are in a very low income area with numerous homeless people. The Management Agent reports that there is a large homeless population in the area and that homeless people often try to occupy areas in the Projects that are not frequently trafficked – and that may provide heat.

5. Holiday 101-A, 1107 West 42nd Street: The Management Agent reports that the damaged roof access door been vandalized and a new one had already been ordered before the inspection. Like the issue discussed above, this damage may have been caused by a homeless person trying to gain access to the roof. In past years, the Projects have encountered significant problems with homeless persons attempting to set up their "homes" on the buildings' roofs.

B. Specific Allegation – Violations Were Caused by Owner's Neglect and Lack of Controls over Maintenance: According to the Draft Report, violations were generally long term in nature, and many were caused by the Owners ignoring HUD requirements and neglecting the Projects for long periods. The OIG also asserts that the Owners did not establish "effective procedures" to monitor the maintenance work, perform preventive maintenance, or perform and document inspections, and these deficiencies contributed to the high number of violations. The OIG also cites alleged failures on the part of the Owners/Management Agent to correct deficiencies identified during REAC inspections.

Specific Response: As further discussed below, this allegation is false.

I. The Owners/Management Agent Had Effective Procedures in Place

The OIG has failed to identify which specific "effective procedures" it asserts are lacking. Among other things, the Owners/Management Agent (1) retained work orders that identified the work to be performed, which performed the work and who the work was approved by; (2) retained inspection reports reflecting the conditions identified upon various inspections; and (3) a maintenance log reflecting the status of various maintenance items. See Exhibit 15. The procedures followed for purposes of evaluating workmen's skills, and tracking, monitoring and evaluating maintenance work, is more fully described at Exhibit 16. Further, the financial statements prepared by the Reznick Firm with respect to the Projects

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confirm that proper internal controls were in place. Therefore, we respectfully request the OIG to (a) identify the particular procedures that it claims are missing, and (b) identify the applicable HUD rule or regulations that imposes such requirement.

II. OIG Has Failed to Recognize the Overall Commendable Condition of the Projects Given the Above-Referenced Circumstances

As noted above, the physical inspection scores for the Projects indicate that, despite the local HUD Office's unwillingness to approve RR account releases and/or rent increases, the Owners and Management Agent have continued to strive to maintain the Projects as required by HUD. In fact, with the exception of Holiday 101B,² the most recent physical inspection reports for each of the Projects reflects a passing score (Holiday 101B missed a passing score by only one point out of 100, and a number of the alleged findings are currently on appeal to HUD). A few additional examples of the physical inspection scores for the Projects received over the past few years is provided below:

75c (Holiday 101A in 2002)
74c (Holiday 101A in 2003)
70c (Holiday 101A in 2004)
93b (Holiday 101B in 2001)
78c (Holiday 101B in 2004)
84c (Holiday 101C in 2001)
93c (Holiday 101C in 2003)
84c (Holiday 102 in 2001)
84b (Holiday 102 in 2003)
71c (Two Worlds II in 2001)
91c (Two Worlds II in 2002)
75c (LA Pro 30 in 2001)
76c (LA Pro 30 in 2002)
89c (LA Pro 30 in 2003)

Regrettably, it is only within the past year, when the impact of HUD's denials of RR releases and rent increases has become particularly acute, that the Projects have struggled somewhat to achieve a passing physical inspection score.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

² We note that the Holiday 101-A Project received a REAC score of 58c in connection with its March 9, 2005 inspection, but that score was increased to 65c in connection with the Project's November 2, 2005 inspection.

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C. Specific Allegation – Section 8 Funds Were Paid for Units in Material Violation: The Draft Report indicates that, based on the inspection results, all of the units sampled would have failed HUD's Section 8 housing quality standards. The OIG asserts that 32 units inspected and another 124 Section 8 units within five of the buildings with the most severe violations materially violated housing requirements. As a result, the OIG concludes \$561,600 in housing assistance payments paid between July 2004 and June 2005 to tenants in units not meeting HUD requirements.

Specific Response. As further discussed below, this allegation is false. As discussed above, REAC inspections evaluating the physical condition of each of the Projects were performed during the relevant years. None of the REAC inspections support the OIG's allegation. The inspections for all of the Projects, but one, reflected a passing score. The one Project lacking a passing score missed by one point out of 100. If the OIG were to apply this standard to all Section 8 projects, a very small number would be able to continue providing affordable housing to needy residents.

Also, as discussed in greater detail above, the physical inspection scores for the Projects indicate that, despite the local HUD Office's unwillingness to approve RR account releases and/or rent increases, the Owners and Management Agent have done a commendable job maintaining the Projects as required by HUD.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

FINDING 3: THE OWNER AND MANAGEMENT AGENT MISMANAGED PROJECTS

A. Specific Allegation – Maintenance Did Not Ensure Maintenance and Accounting Services Were Reasonable: According to the Draft Report, the Management did not sufficiently supervise or control the activities of IOI maintenance and accounting contractors. The OIG, citing Finding 1, asserts that the Management Agent did not follow HUD requirements over procurement to prevent excessive costs and failed to ensure quality work was performed by the maintenance contractor.

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Specific Response: As further discussed below, this allegation is false.

I. Services Were Competitively Bid in Accordance with HUD Contracting Requirements

The Owners/Management Agent contracted for the relevant services on a "competitive basis," per the applicable HUD requirements. The bidding procedures used by the Owners/Management Agent ensured that IOI contractors had to compete with outside contractors to keep costs reasonable. The procurement procedures and controls included, among others, the "Contracting Guidelines" discussed above, as well as other procedures reviewed and approved by the Reznick Group in connection with its preparation of the Projects' financial statements over the past 4 fiscal years.

Over a hundred competitive bids were obtained over the past 5 years in order to ensure that the fees charged to the Projects were "as low as or lower than arms-length, open market purchases." See Owner/Agent Certification, Section 3.d. All such bids were available for the OIG's review during its on-site audit. A sample of such bids was provided to the OIG's staff by Tremelling & Associates (the "Tremelling Firm") on February 1, 2006. A copy of many of the bids is included at Exhibit 1. Although the competitive bids clearly demonstrate the reasonableness of the costs incurred by the Projects, the Draft Report contains absolutely no mention of such bids. In fact, the Draft Report appears to ignore the fact that any such competitive bids even exist.

II. Contracting Procedures and Fees Were Properly Subjected to Annual Review by the Reznick Group

As discussed above, the competitive bidding process used by the Management Agent, and the "reasonableness" of the fees charged by the IOI contractors, were reviewed by the Reznick Group in connection with its preparation of the Projects' 2001 year-end financial statements as well as each of the subsequent years' financial statements. Again, the Reznick Group is a nationally-recognized accounting firm that specializes in HUD's accounting requirements. In response to a finding by a predecessor auditor in its year-end 2000 audit report, the Reznick Group reviewed the bidding process employed by the Management Agent. According to the Reznick Group's records, its review was conducted in order to:

... ensure that [the Management Agent] was complying with the competitive bidding rules required for HUD projects ...and to determine that the amounts charged appeared reasonable." See Exhibit 2.

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The Reznick Group's records indicate that, based upon its review of competitive bids, copies of REAC inspections and follow-up communication, and miscellaneous documentation, "the amounts charged were reasonable" (emphasis added). The Reznick Group further concluded that "any finding or comment relating to excessive charges for maintenance expenses is cleared and is no longer applicable." See Exhibit 2.

In addition to clearing the Finding for fiscal year 2001, the Reznick Group reviewed the reasonableness of the maintenance fees charged, and the relevant procedures, for each of the subsequent fiscal years. None of the subsequent audits raise any findings or other indication that the maintenance charges were somehow unreasonable. Given that the Reznick Group was clearly aware of the issue, and that the firm is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such fees were improper.

III. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

Per HUD Handbook 4381.5, HUD recognizes the essential role that management reviews play in HUD's monitoring of an owner's and management agent's compliance with HUD requirements. See HUD Handbook 4381.5, § 6.21.b. The Handbook further indicates that, in order to properly monitor projects with a management agent performing certain management functions from a centralized location, HUD should conduct management reviews of such projects "at least once every 18 months." Id. at Section 6.33.c. Regrettably, HUD staff did not comply with its own requirement. Management reviews of the Projects were only completed in 1999 and 2002. No subsequent review, other than the OIG audit, has been conducted since 2002. If HUD has objections to the manner in which the Projects were being operated, it certainly would have been helpful if HUD had not waited six years from the 1999 management review – which happened to reflect a "satisfactory" rating – to notify the Owners/Management Agent of such problems. While the 2002 management reviews reflected an "unsatisfactory rating," the transmittal from the Supervisory Project Manager in the HUD Los Angeles Office clearly explains that: "Most of the deficiencies were due to extremely low rents." See Exhibit 3.

Similarly, as reflected in Exhibit 4, the Projects' Management Agent sent numerous letters to Denise Allison, Project Manager, HUD Los Angeles, back in mid-2001 responding to issues raised by the Projects' auditor relating to the reasonableness of fees charged. See Exhibit 4. The HUD Los Angeles Office never responded to any of these letters. We requested the OIG's staff to provide a copy

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of any response that HUD may have provided to the above-referenced letters. The OIG's staff confirmed that it did not have information reflecting any responses from HUD. Again, if HUD had an objection to the Owners/Management Agent's practices, it should not have allowed the practices to continue for many years without raising them with the Owners/Management Agent.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

B. Specific Allegation - Management Charged Ineligible Costs to Projects: Per the Draft Report, the Management charged the Projects for costs already paid through their management fees, including the President's salary.

Specific Response: As further discussed below, this allegation is false.

I. "President" Functioned as Resident Manager/Superintendent

As discussed above, with respect to the Projects, the "President" functions more as a traditional "resident manager" or "superintendent" of the six scattered site Projects. The vast majority of his work involves interfacing with tenants; handling tenant problems; coordinating repairs and replacements; approving moves; inspecting the units, common areas and building exteriors; pursuing tenant fraud and coordinating evictions. These are all front-line activities that are typically associated with a resident manager/ superintendent. The HUD Handbooks expressly recognize, among other things, that salaries paid to a resident manager or superintendent are allowable project expenses. See Industry User Guide for the Financial Assessment Subsystems - Multifamily Housing (October 15, 2004), Item 6330.

II. The Projects Don't Have Any Other Personnel Serving as Resident Manager/Superintendent

The Projects don't have any person, other than the "President," earning a salary that is commensurate with the services required of a resident manager/superintendent. The Projects have a number of "keyholders" that are responsible for reporting any problems to the President. But none of these keyholders perform services akin to those traditionally required of a resident manager/superintendent. Only the President provides such services.

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III. Many of the President's Services are Front Line Costs

The services provided by the President in his capacity as resident manager/superintendent are front-line costs. If the President did not provide these services, the Projects would be forced to pay someone else to do them. The costs of these front-line functions were paid from the Projects' operating account in accordance with its proportionate share of the overall sixty to seventy percent. Compensation for the remaining thirty to forty percent of time was spent performing non front-line functions – and was paid from the management fee.

IV. All Expenses Were Properly Subjected to Annual Review by the Reznick Group

The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the fees charged to the Projects with respect to the President's front-line services. Given that the Reznick Group is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

C. Specific Allegation – Management Charged Ineligible Costs to Projects: Per the Draft Report, the Management charged the Projects for costs already paid through their management fees, including central office costs.

Specific Response: As further discussed below, this allegation is false.

I. HUD Expressly Permits Charges for a Project Office

Reasonable expenses incurred by the Projects for front-line management activities include office expenses associated therewith. HUD's rules recognize that the Projects are permitted to establish a project office as part of the Projects' management cost. The expense for such an office may be properly charged to the Projects' operating account as an administrative expense. See Industry User Guide for the Financial Assessment Subsystems – Multifamily Housing (October 15, 2004), Item 6312

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II. The Centralized Field Office Provides Important Benefits to the Projects

As indicated above, the economic benefits associated with the Field Office should be obvious. It is not economically practical for each of the six Projects to devote one of its rental units to front-line office use. Nor would it be practical to staff a single office for each of the Projects. Such an undertaking would result in front-line costs to the Projects far in excess of their current share of all front-line expenses, including rent, in the operation of the single Field Office.

Moreover, the utilization of the Field Office benefits the project by improving the efficiency of the front-line staff. Historical records as well as current bookkeeping records are near at hand. Oversight of the front-line staff is swiftly and more effectively accomplished. The Field Office is centrally located in a business district and easily reached by the Projects' residents.

III. Rent Charged Was a Reasonable and Necessary Expense

Contrary to the position stated in the Draft Report, the rent for the centralized field office was a necessary and reasonable expense properly charged to the Projects. As discussed above, HUD issuances expressly recognize that the costs related to a "project office" are properly chargeable to a project. See Industry User Guide for the Financial Assessment Subsystems – Multifamily Housing (October 15, 2004), Item 6312.

The rent charged to the Projects for the Field Office was reasonable. The information provided indicates that the total monthly rent charged is about \$0.76 per square foot. When the capital improvements (as further discussed below) are added and spread over the five year life of the Lease, the total monthly cost is about \$1.22 per square foot, which is apportioned among the six projects according to the number of units owned by each.

The information provided further indicates that, in arriving at the amount of the agreed rent for the Field Office, a survey was conducted of fair market rents charged in the area for comparable space. We have been advised that, in 2000, the charge of monthly Field Office rent at \$1.22 per square foot was, and is today, well below the fair market rent for comparable space. The rental rate charged the Projects for its Field Office is a reasonable rent considering the location and activities conducted thereon.

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IV. The Field Office Rent Expenses Were Properly Subjected to Annual Review by the Reznick Group

The Reznick Group prepared the audits for the Projects for fiscal year 2001 and each fiscal year thereafter. As further discussed below, a question was raised by the predecessor auditor in 2000 relating to certain capital improvements to the Field Office. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the field office rental fees charged to the Project. Given that the Reznick Group was clearly aware of the central field office rental expense, and that it is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such rental charges were improper.

V. The Central Field Office is owned by the Projects

As discussed above, the Field Office exists separate and apart from all remaining space on the ground floor of the building in which it is located. The OIG was provided with a copy of the related lease. The Field Office leasehold estate is exclusively owned by the six Projects. The fact that the space is leased rather than owned in fee simple does not negate the fact that the Projects hold a leasehold interest in the Field Office and its improvements.

VI. The Field Office Capital Improvements Were Properly Subjected to Annual Review by the Reznick Group

As discussed above, a finding relating to the capital improvements made to the Field Office was included in the fiscal year 2000 financial audit report for the Projects prepared by John Awad CPA. For the fiscal year 2001, the Reznick Group was engaged as the Projects' audit firm. In that year the Reznick Group cleared the finding made in Mr. Awad's audit report for the Projects. In the Reznick Group's records, the firm explained that: "[c]harges associated with front-line activities at the [centralized field office] are substituted for costs that could be charged if each [of the Projects] had an on-site office space to conduct the business of the [Project]." See Exhibit 14. The Reznick Group concluded by stating:

Based upon a reading of HUD Handbook 4381.5 REV-2, Chapter 6, we believe it is reasonable for the client to allocate these offsite capital improvement charges to [the Projects] and will clear the finding when preparing our 2001 audit reports.
See Exhibit 14.

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The Reznick Group also prepared the audits for the Projects for each fiscal year subsequent to the 2001 audit. At no time did the Reznick Group identify any findings of improper accounting or financial management relating to the field office capital improvements charged to the Project. Given that the Reznick Group was clearly aware of the central field office capital improvements, and that it is a nationally-recognized expert on HUD's accounting and financial requirements, the Owners/Management Agent had no reason to believe any such charges were improper.

VII. HUD Failed to Timely Address Alleged Deficiencies with Owners/Management Agent

As discussed above, in response to questions raised in connection with the 2000 audit of the Projects, the Management Agent sent a number of letters, dated May 25, 2001 and June 11, 2001, to Denise Allison of HUD's Los Angeles Area Office. In the letters, the Management Agent explained that: "The project expenses for the central office costs were tenant improvements for the field office of the scattered sites." See Exhibit 4. In the letters, the Management Agent also explained that the auditor for 2000, Mr. Awad, "had never heard of leasehold or tenant improvements." *Id.* The Management Agent confirmed that, with the exception of the OIG's review during 2005, the issue of the capital improvements was never raised by HUD again. We requested the OIG's staff to provide a copy of any response it may have provided to the above-referenced letters relating to the capital improvements. The OIG's staff confirmed that it did not have a copy of any HUD response to the letters. If HUD had objections to the charges for capital improvements, it most certainly should not have waited nearly 5 years to raise the issue in an OIG audit report.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

D. Specific Allegation - Management Did Not Ensure Projects Were in Good Repair: In the Draft Report, the OIG alleges that the Owners and Management did not operate the Projects in a manner ensuring that they were maintained in good repair as required by the regulatory agreements and other HUD criteria. The OIG asserts that numerous health and safety violations were identified during the OIG's sample inspections. In addition, both Holiday 101-A and Holiday 101-B failed recent REAC inspections.

Specific Response: As discussed in further detail in the Specific Responses set forth above with respect to Findings 1 and 2, this allegation is unwarranted and inappropriate. Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

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E. Specific Allegation – Management Failed to Maintain an Accurate Inventory: According to the Draft Report, the Management Agent did not have an accurate inventory of project appliances and equipment. The OIG indicated that the regulatory agreements require that records over project equipment be maintained in reasonable condition for proper audit. According to the OIG, the Management Agent didn't develop formal procedures and an inventory to track the placement of project assets. The OIG stated that, among other things, the Owners must provide HUD with information on changes or replacement of appliances and items that are normally identified by make, model and serial number.

Specific Response: The Management Agent believes that the OIG only reviewed the handwritten list kept by the maintenance supervisor as his own personal list. The Management Company maintains a separate general ledger which conforms to HUD's requirements. Thus, in connection with the 2002 Management Review of the Projects, HUD's reviewers acknowledge the existence of an acceptable inventory. Specifically, the HUD reviewer responded "yes" to the question: "Is there a satisfactory inventory for accounting for tools, equipment, supplies ...?" Also, the HUD reviewer responded "yes" to the question: "Is a list of equipment and appliance serial numbers maintained?" If the OIG would like to review the above-referenced inventory, a copy will be forwarded under separate cover.

F. Specific Allegation – Management Failed to Correctly Report Excess Income: According to the Draft Report, the General Partner and Management Agent failed to ensure the Projects accounted for \$20,184 in excess income amounts due HUD. The OIG asserts that the lack of reporting and incorrect information appear to be due to the lack of effective procedures and controls to ensure accurate and timely reporting to HUD.

Specific Response: The Owners and Management Agent do not dispute the amount asserted to be due HUD. As discussed above, the Projects have struggled financially due to HUD's refusal to approve much-needed RR account releases and rent increases. Because the Projects do not currently have cashflow available to repay such amount to HUD, and the Projects already owe the Maintenance Company nearly \$590,000 in earned but unpaid fees (as further discussed above), they respectfully request HUD to permit the Projects to retain the above-referenced excess income amount.

Also, please be advised that the Owners have requested the Reznick Firm, the Project's auditors, to assist with ensuring that proper procedures and controls are in place for accurate and timely reporting of excess income.

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G. Specific Allegation – Delinquent Reserve Funds Were Not Reported or Paid: The Draft Report states that the Owner and Management Agent failed to ensure the Projects repaid funds borrowed from the RR accounts. According to the OIG, of the \$705,681 borrowed from the RR accounts, \$81,907 was repaid, \$494,647 was "waived by HUD," and \$129,142 is still owed to the project reserves.

Specific Response: As the OIG correctly recognizes, the Projects were required to withdraw funds from the RR accounts to cover operations due to delays by HUD in making Section 8 subsidy payments. The funds were needed to cover operations and pay certain substantial increases in insurance costs. Contrary to the OIG's allegation, HUD never "waived" amounts owed. Complete HUD 9250's with complete back-up, including cancelled checks, were submitted to, and approved by, the local HUD Office. Rather than receiving the checks from the RR account, the Management Agent asked that the approval be allowed as credits against the RR account disbursements. This procedure was terminated abruptly in December 2002 when HUD stopped all RR account releases until the disbursed amounts were fully restored.

Also, HUD's characterization of the Projects' "borrowing" funds from the RR account is misplaced. The RR account funds belong to the Projects, not HUD. The Projects can not "borrow" their own funds. Regrettably, HUD sought to insist that payments made from the RR accounts be treated as loans – and in so doing, wrongly denied the Projects of much-needed funds that rightfully belonged to them.

HUD's refusal to allow further RR releases was unwarranted and inappropriate given that: (a) the procedure had already resulted in the repayment of nearly \$500,000 of the loans; and (b) three of the six properties had no loans. In November 2002, HUD 9250 requests were submitted for \$12,264 (La Pro 30) and \$8,164 (Two Worlds II). These releases were to be made from the residual receipts accounts and were intended to cover insurance increases. HUD approved these items as "loans," even though the Management Agent protested and HUD has otherwise prohibited the use of use of residual receipts for such legitimate project purposes. See Exhibit 17.

The \$129,142 that the OIG identifies as "still owed" represents monies that were similarly "borrowed" with respect to three of the Projects (Holiday 101-A, Holiday 101-B and Holiday 102) to fund the costs of reasonable and necessary project costs. Again, the Management Agent has previously identified the relevant costs incurred to the local HUD Office and demonstrated that they are reasonable and necessary project costs. HUD has yet to provide any information to the contrary.

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Further, the Owners have confirmed that, through December 2005, the Maintenance Company has not been paid for nearly \$590,000 in fees owed to it with respect to the six Projects. The Maintenance Company should not be forced to continue deferring payment of its fees. Certainly, HUD must recognize that most, if not all, other unaffiliated maintenance companies would not continue working under such circumstances. The financial problems relating to these Projects should not be further aggravated by HUD's refusal to refuse to "waive" RR account releases for \$129,142 in legitimate project costs previously incurred by the Projects.

Based upon the information contained in this Response, we respectfully request the OIG to delete this allegation from the Draft Report.

H. Specific Allegation – Management Did Not Address Obligations to City of Los Angeles: According to the Draft Report, the Owner and Management Agent did not take appropriate action to resolve outstanding obligations to the City of Los Angeles (the "City") for systematic code enforcement ordinance and rent stabilization inspections. The OIG asserts that the lack of payments resulted in the assessment of substantial late charges, which are ineligible expenses.

Specific Response: The City issues bills that include both a "rent stabilization fee" and a "code enforcement fee." The Management Agent has confirmed that project-based section 8 units are exempt from the rent control fees. However, per the Management Agent, the City will not remove the rent control fees without proof of the Section 8 contracts. Since the Section 8 contracts for the six Projects either have no address or a single site address, the Management Agent experienced some difficulty getting the City to confirm that the units are exempt from the rent control fees. According to the information provided by the Management Agent: in January, February and March of 2005, the Agent had an on-going dialog with the City and it felt it had a verbal commitment that the City would waive the late charges and remove the rent stabilization fees. Further correspondence was provided to the City on March 8, 2005. After the March 8, 2005, it appears that the OIG contacted the City and further correspondence from the City stopped (and no response was received to subsequent calls and faxes to the City). See Exhibit 18.

The Owners and Management Agent respectfully request the OIG to (1) allow them additional time to finally resolve this matter with the City, and (2) refrain from taking any action that may prevent a prompt resolution of this matter with the City.

I. Specific Allegation – Project is Missing Support for Note Payable: The Draft Report indicates that the financial statements for Holiday 101-B include a questionable note payable for \$369,578. The OIG states that management could

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Ms. Joan S. Hobbs
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Page 47

not provide support or identification numbers showing the legitimacy of the note and, therefore, it's not clear whether this is an eligible project payable.

Specific Response: The information provided indicates that the note was entered into during the term of the prior management agent. The Management Agent's files do not contain a copy of the note. Also, the Agent has confirmed that no lien is of record securing the note. The Management Agent believes the note relates to a government loan provided to the Project's Owner during the early 1990's in connection with the recovery from an earthquake experienced in the area. The Management Agent has confirmed that it will investigate this issue further. Because the OIG allowed the Owners only a very limited period of time to respond to the Draft Report, the Management Agent has not yet been able to complete its research on this matter. We respectfully request the OIG to defer taking any further action with respect to this allegation until the Management Agent is able to complete its investigation.

CONCLUSION

The Owners and Management Agent appreciate this opportunity to respond to the allegations cited in the Draft Report. As indicated above, the Owners/Management Agent have provided strong evidence to dispute the allegations. They trust that the OIG will ultimately conclude that the Owners/Management Agent acted in compliance with the applicable HUD requirements.

After you have an opportunity to review this Response and the related Exhibits, please call Stephen Niles as (202) 457-7017 to discuss any questions or comments you may have. My clients and I look forward to a prompt resolution of this matter.

Respectfully submitted on behalf of the Owners,

By: 
Holland & Knight LLP

cc: Vincent Mussetter (w/exhibits)
Donald Hollingshead (w/exhibits)

EXHIBIT 9

Response to Allegedly Unsatisfactory Maintenance Work

- A. **OIG Alleges that Maintenance Company's Quality of Work was Inadequate.** The contractor charged the projects for 26 work orders despite unacceptable workmanship.

Specific Allegation: According to the Draft Report, for Holiday 101-C unit D304 and LA Pro 30 unit B209, the contractor claimed to have fixed shower head leaks. This work was charged to the projects respectively in December 2004 under invoice 33228 for \$110 and in March 2004 under invoice 25604 for \$55. However, according to the Draft Report, the OIG's June 2005 inspection of these units found the problems had been "fixed" by the removal of the shower heads without installing new ones in their place, leaving the pipe bare.

Specific Response: The Owners/Management Agent have confirmed the following information relating to the subject unit. Contrary to the allegation made by the OIG, the contractor did not "fix" a shower head leak by the removal of a shower head. Also, work order invoice 25604 does not relate to the repair of any "shower head leaks." Instead, the work order indicates that work was performed to fix leaks at shower handles by replacing seats and washers. Also, work order invoice 33228 states that the repairman replaced the shower diverter because the tenant stated the shower wasn't working.

The Owners and Management Agent acknowledge that the photo included in the Draft Report shows a missing shower head. However, the Management Company has confirmed that as many as 4-5% of the shower heads at the Projects are removed by tenants in order to avoid the use of low-flow shower heads. Regrettably, tenants who dislike the low-flow shower heads often remove the heads in order to increase the water flow. A letter from the unit's tenant, [REDACTED], confirms that she "removed the showerhead in my bathroom so that I could get stronger water when I am taking a shower." See Exhibit 9A.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9A. The documentation includes the following:

Invoice 25604: "Shower leak/removed handle to remove seat and washers; fixed leak also fixed handles."

Invoice 33228: "Repair shower leak and replace shower diverter and repair toilet handle and flapper and kitchen sink leak."

Letter from [REDACTED]: "... I removed the showerhead in my bathroom so that I could get stronger water when I am taking a shower."

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Names have been redacted for privacy

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Specific Allegation: According to the Draft Report, in January 2003, the Maintenance Company began replacing windows for LA Pro 30, 1606 West 47th, unit F111, under work order 8250. The OIG asserts that (a) work did not resume again until December 2 through December 18, 2003, under five work orders, (b) on January 26, 2004, additional work was performed under work orders 16127 and 16114, (c) only two of three windows needing replacement had been replaced, (d) the OIG's June 7, 2005 inspection, a year and a half later, showed the frames had not been installed, and the exterior wood was left exposed (in addition, the windows would not open properly and were not sealed, allowing water to get in), and (e) overall, only two of three windows needing replacement had been replaced. According to the OIG, this work was performed by three of the Maintenance Company's most experienced long-term employees at a labor cost of \$1,212.

Specific Response: The Owners/Management Agent have confirmed the following information relating to the subject unit. Unit F111 is a three-bedroom efficiency unit with five windows – the bedroom/living room has two windows, the kitchen has two windows and the bathroom has one window. The subject building was constructed in 1929 and most of the windows in the units are vintage windows that were not replaced as part of the 1970-71 renovation of the building.

The OIG incorrectly states that "only two of three windows needing replacement" were replaced. In fact, according to the Maintenance Company's records, from January 2003 to January 2004, four of the five windows in the unit were repaired or replaced.

In January 2003, the Maintenance Company replaced the broken window glass in one of the two bedroom/living room windows (see Maintenance Order No. 8250 and Ace Hardware Invoice, Purchase Order No. 2791). This apparently was a simple job and the charge for labor was \$80, which included time spent caulking the tub.

On December 2, 2003, in response to a report that a window in Unit F111 had fallen and broken, the inspection revealed that two of the unit's windows were not in good condition and needed replacement (Maintenance Order 15366). This inspection likely included some temporary measures designed to maintain the habitability of the unit. The labor charge was \$50.

In the afternoon of December 17, 2003 and on the morning of December 18, 2003, one of the vintage kitchen windows was replaced with a 40"X40" glass frame and assembly and one of the vintage bedroom/living room windows was replaced with a 50"X30" glass and frame assembly (see Maintenance Order Nos. 15692, 15699, 15704, Invoice No. 23716, Home Depot Invoice, Purchase Orders, 1497, 1507). The charge for the labor was \$760.

In an effort to balance the importance of habitability and cosmetic considerations with the availability of funds, the work performed on December 17 and 18, 2003, did not include the exterior finishing.

Comment 38

On January 26, 2004, the remaining vintage bedroom/living room window was removed, replaced and reinstalled with new wood interior moldings and sealed (see Maintenance Order No. 16114, No. 16127; Ace Hardware Invoice, Purchase Order No. 1764). The charge for labor was \$322.50.

The replacement of an entire vintage window with a modern type window assembly, like the two replaced in Unit F111, requires considerably more work than simply replacing the glass in an existing window frame. The actual window opening must be enlarged or reduced, depending upon the size of the new window assembly. In many, if not all cases, this requires reframing. Consideration must also be given to the location of plumbing and electrical wiring when undertaking such work. Window openings in pre World War II buildings rarely accommodate new window assemblies without significant carpentry, plaster/drywall and stucco work, inside and out. This Project was no different.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9B. The documentation includes the following:

1/13/03 Work Order 8250:

"Remove the wood moldings and replace new broken window and seal the bathtub."

12/2/03 Work Order 15336:

"Window fell and broke...went to building to check apartment for broken windows, two windows needs replacing, bad condition (partial)."

12/17/03 Work Order 15704:

"Went to building to remove old windows from unit, make new frame for new windows, install new windows secure."

12/17/03 Work Order 15699:

"Installing new windows in kitchen and living room."

12/18/03 Work Order 15692:

"Put one wall around the window then also I patch around the window."

1/26/04 Work Order 16127:

"Remove the bedroom window and replace new window cell (sic), install new wood moldings."

1/26/04 Work Order 16114:

"Went to building to remove window from unit, install new window secure ... put wood molding around window and seal around window."

B. OIG Alleges Maintenance Company left work incomplete.

Specific Allegation: According to the Draft Report, the Maintenance Company did not perform all the work necessary to fully resolve and complete 17 work orders. As an example, the OIG cites bathroom work performed by the contractor on Two Worlds II, 474 Hartford, unit B09, between April 13 and 22, 2004. According to the OIG, the contractor claimed it painted the bathroom under work order 17514; however, the work was not performed as of the OIG's June 21, 2005 inspection.

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Specific Response: The Owners/Management Agent have confirmed the following information relating to the subject unit.

The Owners and Management Agent are unable to confirm the accuracy of this allegation. The Project was condemned in January 2006 by the Los Angeles Unified School District. The School District took possession of the Project in January 2006 and, therefore, the Owners cannot get access to the unit to investigate the matter further.

The Owners/Management Agent have confirmed, however, that the April 2004 Accounts Payable Folder, which contains the relevant work orders and invoices, was not included in the files returned to the Projects by the OIG. Also, it appears that a number of the files returned by the OIG's staff were soaked in water (apparently rain water). Per the Management Agent, the OIG auditor said the files were taken home over a weekend and the auditor got caught in a rain storm without an umbrella. We respectfully request the OIG to provide us with an undamaged copy of the April 2004 Accounts Payable Folder so that the Owners/Management Agent may endeavor to respond to this allegation.

C. OIG Alleges Maintenance Company had to repeat its repairs.

Specific Allegation: According to the Draft Report, there were 69 work orders in which Maintenance Company had to revisit and recharge the Projects to resolve the same issue. The OIG asserts that (a) information showed the contractor had been unable to properly address the problem on its first attempt, which resulted in the Projects incurring additional costs, and (b) if qualified tradesmen had performed the work, the problem could have been immediately resolved and resulted in lower overall charges. For example, the OIG cites LA Pro unit C108 which had a kitchen sink faucet leak repair in January 2004 under Work Order 16125. Per the OIG, the leak was not fixed, and the repair had to be repeated in March 2004 under Work Orders 17520 and 17428 and then again in June 2004 under Work Order 19361. The OIG states that it was not fixed until December 2004 under Work Order 26699. They further claim that the work was performed by three of the Maintenance Company's most experienced, long-term employees for a total cost of \$297 to the project for labor alone. This same unit also had the garbage disposal removed and fixed in January 2004, which had to be done again in March 2004. In addition, the toilet wax ring was replaced in January 2004 but had to be replaced again in April 2004 because it was leaking.

Specific Response: The Owners/Management Agent have confirmed that the work performed on LA Pro 30 unit C108 included all of the following:

- (i) repaired hot water leak kitchen faucet;
- (ii) installed new garbage disposal;
- (iii) replaced shower head;
- (iv) installed new wax toilet ring;
- (v) repaired bath sink faucet;

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- (vi) repaired shower valve; and
- (vii) repaired cold water leak kitchen faucet.

The information provided indicates that the total labor time for all of the above-referenced repairs was 5.5 hours. The Management Agent has confirmed that replacing the wax rings in these 70+ year old buildings is particularly difficult because, among other things, there are often uneven base floors (also, many tenants jar the toilet before it is fully seated). Garbage disposal replacement can also be difficult because the plumbing is almost 40 years old and should be replaced. A mid-term rent increase request was presented to HUD in October 2002, identifying the repair and replacement costs required in these buildings. This request was denied. Additionally, numerous letters to various HUD officials were sent documenting the properties' needs and the distress of HUD "freezing" the reserve accounts.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9C attached. The documentation includes the following:

1/26/04 Work Order 16125:

"Repair kitchen leak hot water fixit" It indicates two seats and two washers in kitchen sink were replaced. (30 min. repair time).

1/27/04 Work Order:

"Remove garbage disposal and install garbage disposal; replace new shower head; remove the toilet and install new wax [ring toilet]" (2 hrs. repair time).

3/17/04 Work Order 17520:

"Repair bathroom sink faucet, shower valve, kitchen faucet leaks ... removed garbage disposal and install back" (1 hr. repair time).

4/19/04 Work Order:

"Replaced wax [ring] toiled ... sealed" (2 hrs. repair time).

D. OIG Alleges Maintenance Company charged for questionable lock repairs.

Specific Allegation: According to the Draft Report, there were 101 work orders for lock repairs and similar work that did not appear reasonable and necessary due to their unusual frequency on the same units. The OIG asserts that LA Pro 30 unit B203 had 11 work orders to repair entrance door locks between January 2004 and May 2005, costing the project \$605. According to the OIG, the tenant occupying the unit since 1996 had no knowledge of this work. In addition, Holiday 101-C unit B3-5 had 12 work orders between April 2003 and November 2004 to repair the entrance door locks and program phone numbers into the intercom, costing the project \$642. According to the OIG, since on site managers have copies of the keys for lockouts, "it isn't clear whether this work was necessary or performed."

Specific Response:

LA Pro 30 unit B203: The Owners/Management Agent have confirmed the following information relating to the subject unit.

Comment 41

The tenant in this unit since 1996, [REDACTED], doesn't speak nor understand any English or Spanish. The Management Agent believes that the OIG auditors must have spoken with one of [REDACTED] numerous guests rather than with [REDACTED]. The Management Agent has confirmed that this resident has had many "problems" with his locks, many of which are centered on his numerous guests. The information provided by the Management Agent identifies the various repairs performed during the relevant time period:

- (i) lost keys (rekeyed);
- (ii) lost keys (rekeyed);
- (iii) picked locks for maintenance emergency;
- (iv) latch stuck;
- (v) locked out;
- (vi) lubricate locks;
- (vii) latch stuck; and
- (viii) replaced lock.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9D.

Holiday 101-C unit B305: The Owners/Management Agent have confirmed the following information relating to the subject unit.

The unit was occupied during the relevant period by [REDACTED]. [REDACTED] was evicted in July 2005. The Management Agent confirmed that it had many problems with [REDACTED], apparently vandalizing his own unit. [REDACTED] reported many incidents of his unit being entered, "break-ins", and his locks being vandalized. The Management Agent was notified by counsel that, in such circumstances, the Management Agent should not pursue an eviction until all maintenance requests are satisfied. Thus, the Management Agent made repeated efforts to resolve problems with the locks claimed by [REDACTED].

Comment 42

Also, the Owners/Management Agent have indicated that they are confused by the OIG's statement that: "...since on-site managers have copies of the keys for lock-outs, it isn't clear whether this work was necessary or performed." Phone number programming for the entrance intercom is intended to permit residents to let guests enter the building; it is unrelated to lock-outs. Clarification on this allegation is requested from the OIG.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9D. The documentation reflects the following:

12/5/03 (#23461)	repaired entrance door locks	Labor \$50.00
2/9/04 (#24877)	repaired entrance door locks	Labor \$55.00
3/8/04 (#25622)	repaired entrance door locks	Labor \$55.00
5/20/04 (#27707)	repaired/rekeyed entrance door locks	Labor \$55.00

7/13/04 (#29181)	programmed telephone number on intercom	Labor \$65.00
7/22/04 (#29455)	repaired entrance door locks	Labor \$55.00
8/30/04 (#30535)	repaired entrance door locks	Labor \$55.00
9/7/04 (#30735)	program telephone number on intercom	Labor \$27.50
11/22/04 (#32851)	repaired entrance door locks	Labor \$55.00
12/9/04 (#33284)	repaired entrance door locks	Labor \$55.00
1/27/04 (#24563)	repaired entrance door locks	Labor \$55.00
4/7/04 (#26514)	repaired entrance door locks	Labor \$55.00
4/27/04 (#27088)	repaired entrance door locks	Labor \$55.00
6/17/04 (#28498)	repaired entrance door lock and key got stuck	Labor \$55.00
7/14/04 (#29227)	repaired entrance door locks	Labor \$55.00
9/2/04 (#30660)	repaired entrance door locks	Labor \$55.00
10/1/04 (#31433)	repaired entrance door locks	Labor \$55.00
10/14/04 (#31798)	repaired entrance door locks	Labor \$55.00
12/21/04 (#33602)	repaired entrance door locks	Labor \$55.00
1/14/05 (#34325)	repaired entrance door locks	Labor \$55.00
5/11/05 (#37852)	fixed lock on security door	Labor \$55.00
5/25/05 (#38317)	fixed entrance door locks	Labor \$55.00
11/22/05 (#45233)	fixed entrance door locks	Labor \$55.00

E. OIG Alleges that Management Agent could not produce all work orders.

Specific Allegation: According to the Draft Report, the OIG requested all invoices and work orders associated with maintenance work performed since 2003 on the units inspected. Although most invoices and work orders were available, the OIG asserts that (a) that documentation for 97 separate charges to the projects was missing, (b) the only information available was invoice data in the management agent's Quickbooks accounting system, and (c) the OIG could not determine exactly what was done or who performed the work.

Specific Response: The Owners/Management Agent have confirmed that four of the Management Agent's employees made every effort to respond promptly to all of the OIG's requests for work orders. Tens of thousands of work orders were made available to the OIG for its review. Even assuming the OIG's allegation is correct, the 97 missing work orders represent an extremely small percentage of the total number of work orders. If the OIG will provide additional information relating to the 97 work orders at issue, the Owners/Management Agent shall undertake to locate the work orders and provide them to the OIG.

F. OIG Alleges Maintenance Company charged for other questionable work.

Specific Allegation: The OIG claims that nineteen work orders included various issues making work performed "appear questionable." The OIG cites repairs to LA Pro 30 unit F111 under Work Order 9390. According to the OIG, the Work

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Order indicates that a paper holder rack was replaced as of January 2003 for \$50. However, as of the OIG's June 2005 inspection, there was no applicable paper holder rack in the unit.

Specific Response: The Owners/Management Agent have confirmed the following information relating to the subject unit.

The information provided indicates that the tenant of the subject unit, [REDACTED], moved into the unit on January 17, 2003. The Management Agent confirmed with [REDACTED] on January 31, 2006 that she has always had a paper holder in the unit. Therefore, the Owners and Management Agent request further clarification on this allegation from the OIG.

A copy of the documentation referenced in this Specific Response is included as Exhibit 9E attached. The documentation includes the following:

1/10/03 Ace Hardware Invoice:

"Paper holder.

1/10/03 Invoice:

1/10/03 Maintenance Order:

"Replaced paper holder (rack)."

Note indicating "tenant ... [REDACTED] stated 1/31/06 that both the toilet paper holder and rack have been and still are there."

G. OIG Alleges Inadequate Monitoring of Maintenance Work Performed by the Maintenance Company.

Specific Allegation: According to the Draft Report, the Owner and Management Agent did not monitor maintenance performed by the Maintenance Company to ensure the work was properly completed. The OIG asserts that: (a) the Owners and Management Agent did not require the IOI contractor to implement a satisfactory maintenance work order system to ensure all necessary repairs were adequately addressed, (b) there was no log to identify and track tenant requests or deficiencies identified during inspections, (c) there was no system to ensure work orders were completed within a reasonable timeframe for a reasonable cost, (d) there was no evidence the maintenance supervisor evaluated the performance of the staff or verified the skills of new employees, and (e) although the maintenance supervisor was a licensed contractor, he was inexperienced at running a maintenance company.

Specific Response: The Owners/Management Agent have confirmed that maintenance logs are maintained with respect to the maintenance work performed by the Maintenance Company. Exhibit 9F includes (1) a sample of the maintenance logs used; (2) a sample of the work orders reflecting the work performed and review and approval of such work; and (3) a summary of the

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▶	
▶	procedures followed for purposes of evaluating workmen's skills, and tracking, monitoring and evaluating maintenance work.
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Holland & Knight

Tel 202 955 3000
Fax 202 955 5564

Holland & Knight LLP
2099 Pennsylvania Avenue, N.W., Suite 100
Washington, D.C. 20006
www.hklaw.com

Stephen D. Niles
202 457 7017
stephen.niles@hklaw.com

February 23, 2006

VIA ELECTRONIC MAIL AND FEDERAL EXPRESS

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

Re: Discussion Draft Audit Report (January 19, 2006)
Holiday Apartments, Two Worlds II and LA Pro 30 (the "Draft Report")

Dear Ms. Hobbs:

As a follow-up to the Response that I sent to you, dated February 21, 2006, relating to the above-referenced Draft Report, please be advised that information responding to one of the allegations included in Finding 1 was omitted from the Response. The allegation pertains to alleged incomplete work on Two Worlds II, 474 Hartford, Unit B09 (see Page 12 of Draft Report). The attached "Exhibit 19" includes the relevant information responding to the allegation.

I understand, of course, that your office wants to ensure that it reviews all of the relevant information responding to the Draft Report. Therefore, please insert the attached Exhibit 19 in the Response and include it as part of your review.

Respectfully submitted on behalf of the Owners,

By: 
Holland & Knight LLP

cc: Vincent Mussetter (w/exhibits)
Donald Hollingshead (w/exhibits)

EXHIBIT 19

RESPONSE TO DRAFT AUDIT FINDING 1
PAGE 12

Comment 44

* Action Maintenance left work incomplete.

O.I.G. Finding: The Draft Audit states that "Action Maintenance did not perform all the work necessary to fully resolve and complete 17 work orders. For example, bathroom work was performed by the contractor on Two Worlds II, 474 Hartford, unit B09, between April 13 and 22, 2004. The contractor claimed it painted the bathroom under work order 17514; however, the work was not performed as of our June 21, 2005, inspection (see photograph of bathroom ceiling)."

Response: This matter was partly addressed in our response to the Draft Audit served by E Mail on February 21, 2006 (the "Response"). As pointed out in the Response, adequate time to respond was not permitted by the I.O.G. notwithstanding our timely requests.

Initially the Owner/Management Agent were placed at a distinct disadvantage by the O.I.G.'s failure to return to Work Order 17514 and other maintenance records bearing upon this issue that were timely provided by Action Maintenance. However, since the service of the Response our continuing investigation has uncovered additional, relevant documentation and information.

It now appears the Draft Audit claim that the bathroom paintwork was not completed during the 14 month period after work was commenced is false.

Contrary to the Draft Audit finding, we now confirmed that painting of the bathroom and other areas of Unit B09 was commenced and completed on April 13, 2004 as recorded in Work Order 17514 (Exhibit 19).

It is true that the O.I.G.'s physical inspection of Unit B09 conducted on June 21, 2005 correctly revealed areas of the bathroom ceiling not covered with paint. A careful examination of the photo contained in the Draft Audit shows a section of unpainted drywall and areas of patching.

The O.I.G. was apparently unaware that its physical inspection observed the repair of recent water damage to the bathroom ceiling undertaken on June 8, 2005, shortly before the inspection.

The recently located records of the Owner/Management show that the repair of water damage included the installation of drywall and patching performed on that date (Exhibit 19).

The Draft Audit is therefore highly misleading in suggesting that the repairs of Unit B09 illustrate the failure of Action Maintenance to "fully resolve and complete 17 work orders."

OIG Evaluation of Auditee Comments

- Comment 1** We allowed reasonable time for the exit conference, and the auditee had a month to prepare its written response. In addition, the auditee had been provided draft finding outlines between August 22 and December 6, 2005, identifying finding issues, which included notifying the auditee that maintenance costs were excessive when compared to a construction cost index.
- Comment 2** The background section of the report discussed recent Real Estate Assessment Center inspection results.
- Comment 3** Matters regarding the central office were referred to OIG by the HUD Los Angeles offices indicating resolution had not occurred.
- Comment 4** Where Reznick Group may have experience and expertise in auditing HUD insured projects, we can only rely on our own testing of compliance with federal regulations, which is generally more extensive than the testing for compliance in financial audits.
- Comment 5** We will address individual violations below. Each violation identified in this report is contrary to a HUD handbook or regulatory agreement requirement. The project ownership signed the regulatory agreement, which stated it would comply with HUD's requirements as well as those contained within it. Since the ownership signed the document, it is assumed to know what is in it and, therefore, willingly violated its requirements.
- Comment 6** The supervisory staff the OIG spoke to were the President and the Controller of Proland Management Company, which is also the parent company of the bookkeeping companies. The same two individuals also hold the same supervisory positions with Proland Real Estate, which does business as Action Maintenance.
- Our intent is to gain compliance with HUD's requirements and return the project to its original state, had violations not occurred. We do not wish to remove affordable housing from the market. Additionally, we have not recommended such sanctions and they are not even available under chapter 7.4 of HUD Handbook 4381.5 REV-2. We appreciate that the owners wish to work with HUD to correct violations.
- Comment 7** The specific references within the handbook were left out to make the report easier to read. It is clear from the direct references in the auditee's comments, the auditee has identified the specific criteria within the handbook so no further adjustments were made to the report.

Comment 8 In addition to the management agent’s certification and HUD Handbook 4381.5, the regulatory agreements require project costs to be reasonable and necessary. We have demonstrated in our report where we do not believe the owners and management agents complied with this provision even when obtaining bids.

Comment 9 The exhibit provided, which is supposed to show that the Reznick Group performed its own bid testing and determined the amounts were reasonable, is an unsigned and undated “MEMO TO FILE.” It has no information showing it was prepared by Reznick and included in its audit workpapers. There is also insufficient information to show what detailed testing was performed, or how the conclusion was reached. As a result, we cannot rely on the results. We can only rely on our own testing performed during this audit, which is usually more thorough than the compliance testing performed in financial audits.

Comment 10 Although the auditee claims it obtained over 100 competitive bids, 33 were provided to our office relating to repair services (along with several duplicates of some bids).

Discussion with the President of Proland Management had indicated bids were obtained in relation to Action Maintenance procuring for services that it could not perform and costing over \$2,000, as stated in the auditee’s disbursement procedures. The bids were not presented as the justification for using Action Maintenance’s services. However, we have reviewed the bids provided by the auditee. The majority of the bids were obtained by Action Maintenance, the company the bidders would supposedly replace, which would demonstrate poor management practices and makes them questionable. In addition, the majority of the bids were for licensed professionals, such as plumbers, electricians, and carpenters, specialists that Action Maintenance did not employ. In addition, most of the rates were for single services, not what a vendor would necessarily charge under a long term contract. Finally, the rates on the bids would be higher to compensate the vendor for travel time to the site, as opposed to charging directly for the travel time; whereas Action Maintenance charged the projects its full hourly rate for all time and travel on any job.

The auditee only produced 5 bids from maintenance companies that were similar to the services performed by Action Maintenance. One was an undated bid submitted by the former supervisor for Action Maintenance, which was therefore unreliable. The remaining bids listed rates of \$25 to \$42 per hour as their average hourly rates (not including travel). The maintenance bids included one obtained in 2000, none between 2001 and 2003, one in 2004, and two in 2005, which would not meet the minimum threshold of obtaining 3 applicable bids per year.

In addition, one of the 2005 maintenance bids, which listed its individual service call rate at \$35 per hour, recommended “it would be more economical to work under a maintenance service contract” in which the vendor offered a flat fee of \$3,500 per month for all repairs on up to 700 units, excluding materials. Action

Maintenance's average monthly cost to address the projects' 632 units was \$56,090 (excluding materials), far higher than the proposed rate.

- Comment 11** Based on discussions with the HUD Los Angeles offices, limitations or denials for rent increases and/or withdrawal requests from the reserve for replacement accounts were due to the owner's and management agent's noncompliance with HUD requirements, issues leading to the referral to the OIG.
- Comment 12** The letters were not identified in HUD's files, so we do not have any information to show that HUD received the letters in question or responded to them. However, issues discussed in these letters were later referred by HUD to the OIG for further review. The OIG is independent of HUD and HUD does not bring about issues in our report. We are only reporting on violations of regulations we identified during our audit.
- Comment 13** The handbook requires written cost estimates from vendors for any ongoing service that is expected to exceed \$10,000 per year. The projects paid for maintenance services in excess of this amount and, therefore, the overall maintenance service for the year should have been bid, not the cost of individual jobs as was done. The service would need to be sent out for bid every year after that or brought in-house and performed by project employees. Had this been done, the owner would only need to maintain three years of bidding documentation. If a five-year contract had been signed, the bids would have needed to be maintained for five years or the length of the contract. As it is currently, there is no assurance the maintenance services provided were at the most reasonable cost.
- Comment 14** In addition to the procurement and bidding requirements detailed in the management agent's certification and HUD Handbook 4381.5, the regulatory agreements require costs to be reasonable and necessary. In the absence of adequate applicable bids for long-term maintenance services to show the identity-of-interest contractor's costs were reasonable, we determined what the reasonable cost would be from other sources.

We reviewed personnel records, payroll, and Action Maintenance's unaudited financial records to determine what their actual costs and profit were in performing the services for the project, and noted the profit margins were excessively high. This was corroborated by the large transfers of cash from Action Maintenance to the owners, ranging from \$420,000 to \$832,000 each year between 2000 and 2005.

We also checked a standard cost index used by contractors and appraisers to determine construction related costs. These amounts are not "guesses" as contended by the auditee, but based on information obtained by the vendor on actual wages rates. The higher rates provided by the Saylor Cost Index for professions such as electricians, plumbers, and carpenters would not apply to

Action Maintenance since the contractor was not employing such skilled workers to address its work orders. The higher rates charged by independent contractors for those professions directly relate to the higher salary such skilled and licensed workers command. Whereas Action Maintenance's average employee earned around \$11, and its highest paid worker earned \$18 an hour as of 2005, the base wage for an open shop electrician and plumber approached \$37 and \$31 per hour. Although its employees are generalist performing a variety of maintenance functions, the identity-of-interest relationship between the owner of the projects, the management agent, and the maintenance contractor, allowed Action Maintenance to charge the projects for rates approaching licensed craftsmen.

Although HUD doesn't specifically limit the owner's profit margin, costs must be reasonable and necessary in accordance with the regulatory agreement.

Comment 15 Although the maintenance supervisor was a licensed contractor, as mentioned in the report, he was not addressing the maintenance work orders in question. In addition, the six employees listed by the auditee were the most skilled of the contractor's 65 employees working during various periods between 2000 and 2005. Our review of personnel files showed the staff were generally hired as maintenance employees, not plumbers or electricians, with no mention of electrical certifications or training. Although the auditee has provided new resumes for these maintenance staff, and provided support that one was a locksmith, there has been no support provided to show that the remainder were licensed electricians or plumbers.

Comment 16 The example provided by the auditee uses the highest pay rate paid to any of its employees between 2000 and May 2005, when the majority of the maintenance staff earned less than \$11 per hour. We confirmed the health cost and payroll tax matched the rates listed by the auditee. However, review of Action Maintenance's actual costs show its average per hour cost would be \$0.22 for car allowance, \$1.20 for leave and holidays, and \$1.07 for workers compensation, lower than the rates listed by the auditee. Also, since Action Maintenance charges a higher rate for actual overtime worked, adding a factor of \$1.16 to the base rate would not be reasonable. In addition, even using the auditee's own numbers for its highest paid employee, the maximum rate of \$38.30 (which includes overhead and profit) is significantly below the \$55 per hour charged to the projects.

However, upon further consideration, we noted the Saylor open shop rates did not clearly identify the inclusion of fringe benefits into their calculations. Although not all of Action Maintenance's employees received these fringe benefits, we have made an allowance for leave, holiday pay, and health benefits based on Action Maintenance's costs and policies. This has increased the projected reasonable rate to \$25 per hour, which is also in line with some of the maintenance rates included in the documentation provided by the auditee. We adjusted the report wherever necessary.

- Comment 17** If the maintenance contractor performed the alleged services, the maintenance contractor should have properly invoiced the projects for actual work performed. The management agent should not have allocated the maintenance supervisors costs to the projects as if he were a management agent employee performing front-line activity, with no record concerning the time spent performing those activities. We also noted that exhibit 6 did not include inspection reports to support the auditee's assertions, and only included work orders signed off by the subsequent maintenance supervisor (not the maintenance supervisor in question).
- Comment 18** The maintenance contractor did not keep track or bill based on actual work performed. The one example of an invoice provided by the auditee did not show what work was performed. Our office had previously requested inspection reports, which were not provided. In addition, there were no examples of inspection reports under exhibit 7. However, the auditee did submit a 2006 work order provided under exhibit 15 showing one of the maintenance staff "went to check the jobs that are finished and the jobs that need to be done in the properties" instead of the maintenance supervisor. Exhibit 15 also included one example of a building inspection report from February 2005, but it was prepared by one of the maintenance workers and not the maintenance supervisor. Finally, there was a single example of a vacant unit inspection report provided, prepared in November 2005 (after our audit period), but it was signed by someone other than the maintenance supervisor.
- Comment 19** The report has been adjusted to discuss the bids obtained by the management agent. However, we have not been provided bids over materials purchased in volume. If third parties were selected to perform work, they should have been contracted by the management agent and not the maintenance contractor. Using the identity-of-interest maintenance contractor to perform services which are the management agent's responsibility, and charging additional fee for it, would not be reasonable.
- Comment 20** We cannot ignore violations of health and safety requirements identified during HUD OIG inspections simply because the projects passed prior Real Estate Assessment Center inspections.
- Comment 21** The 2001 memo was issued during the audit period in question and has not been revised, so it is therefore applicable. The document established what HUD considered a reasonable median amount for bookkeeping fees. The subsequent San Francisco memo was also provided to the auditee after the exit conference because it came up during the discussion, and to demonstrate the limitation applies to other areas and later periods.
- Comment 22** Following the exit conference, we provided the auditee detailed schedules showing how the amount was computed, and also provided copies of the

auditee's own vendor ledgers and invoices from which the information was obtained (per their request).

Based on our discussions with the two staff members in question, they primarily worked on bookkeeping related functions not occupancy functions. Different Proland Management staff performed the occupancy functions.

Comment 23 The bookkeeping "bids" provided were primarily resumes and letters from placement and temporary agencies, all obtained around the end of 2000. It appears these persons were trying to obtain employment with Proland Management instead of contracting for a service. In fact, one mentioned they had read Proland's add in "the LA Times for the accounting position." As a result, these are not true bids for service.

The hourly rates were generally not listed by the applicants but written in by unknown person(s). There was no information to show how many hours an actual contractor would have charged to perform the service, to be applied to the identified rates. Since the bookkeeping charges performed by the identity-of-interest contractor were fixed and not charged on a per hour basis, we cannot compare these costs to the "bid" rates. However, a document previously provided by the auditee showed a consultant previously proposed performing the project's bookkeeping for \$3.50 per unit per month, which would have been substantially less than charged by the identity-of-interest contractor.

Comment 24 The actual bookkeeping costs can be charged to the project if the costs do not exceed the cost of independent vendors to perform the function, subject any cap set by HUD to ensure these rates are reasonable. The auditee has not adequately shown what contractors would have charged, nor were subsequent bids obtained in subsequent years. In addition, since the owner was directly charging the project for the payroll of staff performing bookkeeping functions, the amounts paid to the identity-of-interest contractor are unnecessary duplicative costs.

Comment 25 The add on fees mentioned under Handbook 4381.5 are for additional travel costs associated with scattered site properties and/or maintenance costs in adverse condition neighborhoods, which should not be allowed if already covered under the project's residential management fee. The item cited by the auditee was not related to bookkeeping.

Comment 26 The auditee is now retroactively down-grading the President's position to "resident manager/superintendent," even though he has acted as the Management Agent's representative to HUD, performed supervisor management agent functions, and has not previously been represented as merely a resident manager. The position of a resident manager also denotes that he actually lives at the projects in question, to which we have been provided no support.

The management agent's organizational chart also showed all employees reporting to the President. Also, as mentioned in the report, the job description of the President included supervisory roles such as overseeing staff, setting policies and procedures, approving payroll, and acting as liaison with HUD. Only after the draft report was issued has the auditee included an extra page to the President's position description, which now includes additional non-supervisory activities to make his position appear to be a generalist. However, HUD Handbook 4381.5 still prohibits generalist staff performing front-line costs from performing supervisory functions.

Although we had requested documentation to support the President's charges during the course of the audit, monthly timesheets were only provided until the auditee issued its response to the report. HUD Handbook 4381.5 states the hours spent performing front-line activities should be documented on weekly timesheets. In addition, the hours listed on these monthly timesheets, although varying each month, were still allocated to the projects at the same percentage each month. Also, if the auditee believes it was appropriately charging the projects, it isn't clear why the charges suddenly stopped in September 2004, when there is no evidence his position or activities changed.

Finally, several of the items listed as front-line activities also appear questionable. The President lists a number of hours dealing with residents, recertifications, and their paperwork even though the management agent employs occupancy specialist and maintains resident manager "keyholders." He also lists he was performing property level bookkeeping and posting accounts payable even though there was an identity-of-interest contractor and other staff being charged to the projects for performing these functions. In addition, he lists property level inspections even though Action Maintenance's supervisor was supposed to be performing this function (the President did not attend any of the OIG inspections). Finally, a number of hours were designated as budgeting, even though Handbook 4381.5 states preparing budgets required by the owner or HUD, exclusive of rent increase request and MIO plans, is covered by the management fee.

Comment 27 After further consideration, we have adjusted the report to show the rent and capital improvement charges as unsupported. Although it may be allowable to charge central office costs of eligible front-line staff to the projects, the costs should be reasonable and necessary in accordance with the regulatory agreement. The lease agreement between the project and the management agent allocates a disproportionate amount of the actual building's cost to the projects. A reasonable amount would be based on the amount the owner/management actually pays for the building. Any allocation of that cost should be based on the actual space necessary for the eligible front-line staff. Any improvements to the office charged to the projects should be reasonable charges for improvements to the space required by those persons to perform their front-line activities. Currently, there is insufficient information available to determine the actual space needed

by the eligible front-line staff, and which improvements were for their space, as opposed to the owner's, identity-of-interest contractors', or the management agent's space.

Comment 28 The spreadsheet included in the report clearly designates the entities in question, and the year in which the payments were made. During the exit conference we offered to provide the auditee with our calculations and support on finding issues. No requests were made for the amounts in question. However, we can provide the auditee with additional information upon request.

Comment 29 The projections of ineligible costs were made to ascertain the potential future inappropriate activity continuing after our audit period. Although the auditee does not have to return the estimated amounts, as part of our audit recommendations, HUD should determine the subsequent ineligible costs charged to the project and require repayment.

Comment 30 HUD Handbook 4381.5 requires the projects to be in compliance with Housing Quality Standards, which were the standards applied in determining whether a unit or building passed or failed the inspection. The Real Estate Assessment Center uses Uniform Physical Condition Standards for the basis of their inspections. The inspections are used as a tool by Multifamily to monitor the physical status of their insured portfolio, not to ensure the project is in compliance with its requirements to maintain its housing in accordance with Housing Quality Standards. The violations themselves would be health and safety violations under both Housing Quality Standards and Uniform Physical Condition Standards.

Comment 31 The issues were designated as health and safety violation by the OIG's certified appraiser.

Comment 32 We requested inspection reports from the auditee during the course of the audit, and were specifically informed these documents were not prepared. Only one building and one unit inspection report was provided as part of the auditee's response, one of which was prepared during the course of our on-site work and the other after we completed on-site work.

The maintenance log provided only covers selected periods up to 2003, and does not show when and if the work was completed or which work order it was performed under. The President and Controller (these two individuals are also the President and Controller of Proland Real Estate, which does business as Action Maintenance) specifically told the OIG that Action Maintenance was not tracking tenant requests, there was no process to prevent duplicative charges of work orders, and completed work orders were not organized by unit or tenant.

Comment 33 We were specifically told by the President and the Controller of Proland Management that there was no such inventory over appliances. The one page example now provided by auditee does not appear current.

Comment 34 We have amended the wording of the report to state the amounts were *credited* against the loan balances.

Reserve for replacement funds are restricted escrow and releases must be approved by HUD. Due to the restriction on the funds, they can be borrowed for unrestricted purposes as was the case here. Additionally, this transaction is further defined as a loan because the terms of repayment were defined.

Comment 35 Per the auditee's request during the course of the audit, we did not contact the City of Los Angeles concerning the obligations.

Comment 36 The auditee was notified the loan and support was requested in March 2005. This should have been sufficient time to obtain the documentation. If support is found, resolution of this matter can be coordinated with the HUD Los Angeles office.

Comment 37 The tenant of B209 had confirmed that maintenance had also performed work on the shower wall, and in doing so Action Maintenance had removed the shower head. The wording of the report will be adjusted to reflect this.

The work order for D304 had not been provided when originally requested. It states the shower leak was repaired and the diverter was replaced.

The auditee included a tenant's statement claiming the tenant removed the shower head. However, this tenant did not occupy either of the two units in question, B209 or D304; instead she resided in unit F111. The OIG inspection of F111 showed the unit had a shower head, so it is unclear how the owner obtained this statement or why the tenants made these comments.

We discussed the matter of tenants removing shower heads, preferring to have the water come directly from the pipe, with the OIG appraiser. Throughout his various unit inspections he has not seen this as a practice of tenants.

Comment 38 There were five windows in the zero bedroom unit, one in the bathroom, two in the living room/bedroom, and two in the kitchen. The inspection showed two windows had been clearly replaced (not three as contended by the auditee), and at least one other clearly needed work but hadn't received any. In addition, the support provided for the January work orders only showed \$10 of materials purchased, which would have been insufficient to replace a third window.

Initially, it appeared the window installed in January 2003 was the one that subsequently fell out, as reported in the subsequent work order. However, upon further consideration, it may have been one of the other windows so we have removed that work order from the report. The remaining work orders remain questionable as the work was poorly performed and left incomplete.

Comment 39 No original documentation has been retained by the OIG. No documentation would have been removed from the agent's office except with the express permission of the management agent.

Comment 40 The information provided does not address why it required so many attempts to fix a kitchen sink leak. We discussed the setting of toilets with the OIG appraiser, who advised if a toilet is properly set and secured, a tenant should not be able to accidentally jar it loose.

Comment 41 The tenant of unit B203 understood enough English to speak with, and even verified the amount of rent paid for the unit. For unit B305, no documentation, such as police report or tenant complaints, has been provided to demonstrate reports of break-ins or locks being vandalized. The information now listed by the management agent in the auditee's response was not reflected on the work orders and invoice documentation during our audit. Further, it does not explain the high frequency of work on the units' locks.

The reference to the on-site managers having keys was related to whether it was necessary to require maintenance to come to the unit for a simple lock out.

Comment 42 We requested work orders for the units as we informed the management agent of which tenants to notify, at least six to twelve calendar days before the respective inspections. The short notice was to prevent the auditee from targeting units it knew we would inspect just to correct existing problems (note: the list for 2005 work on Two Worlds II unit B09, provided as part of the auditee's response, shows maintenance did target the unit one day prior to the OIG inspection to "reinstall smoke alarm, fixed stove burners"). If the management agent maintained the documentation in order, the work orders should have been readily available. However, as the President of Proland Management informed us, the work orders were not organized by unit or tenant. In addition, the missing invoices were significant, representing 11 percent of the amount charged for all work orders requested.

Comment 43 We accept the auditee's response to the paper holder, and it has been removed from the report.

Comment 44 The auditee provided another response on February 23, 2006. The auditee stated that work relating to unit B09 was completed, and that the ceiling work had just been performed on June 8, 2005 just prior to our June 21, 2005 inspection. The auditee provided a new list of work orders from their system showing this work, but not the actual work orders themselves. If this information is accurate, the unit still remained unfinished at the time of our inspection, and the auditee's additional records show no painting occurred at least until November 2005, when Action Maintenance again fixed the bathroom ceiling. However, even the listing for

the November work did not mention any painting took place. Also, the attaching of drywall on top of existing drywall does not demonstrate good workmanship.

Appendix C

STATISTICAL SAMPLING METHODOLOGY

We used the Texas State Auditor's Office Statistical Sampling Tool and Audit Command Language to perform statistical sampling calculations so that we may use the results from the sample to project the rate of occurrence to the universe from which the sample was drawn. Using these software programs we were able to review a reasonable number of project-based Section 8-subsidized units managed by Proland Management Company, determine whether these units had inappropriate health and safety violations which would fail HUD's housing quality standards, and project with a high degree of accuracy to the universe of 609 Section 8 units.

Using the statistical sampling tool with a confidence level of 90 percent, an expected error rate of 50 percent, and desired precision of 10 percent, we calculated that a sample of 60 would be appropriate. Attribute sampling tests whether a particular condition in the universe exceeds a specified acceptable level. In this instance, the condition was whether the Section 8 unit met housing quality standards through the absence of health and safety violations.

The management agent provided form HUD-50059, Owner's Certification of Compliance with HUD's Tenant Eligibility and Rent Procedures, for March and May of 2005, listing the Section 8 units for Holiday Apartments (101-A, 101-B, 101-C, and 102), LA Pro 30, and Two Worlds II. We selected the sample of 60 units, along with 25 backup units, at random without bias using Audit Command Language. The backup samples were selected as replacements in case we were unable to inspect any of the first 60 units and would be reviewed in the sequence selected by the software. However, we were able to inspect all 60 units so no backup units were reviewed.

Appendix D

SCHEDULE OF INSPECTION RESULTS

Sample item	Property	Street address	Unit	Pass/fail housing quality standards	24-hour violations	10-day violations	30-day violations	Total violations
Building 1	Holiday 101-A	1102 West 41st Place		Fail	6	0	2	8
Unit 1	Holiday 101-A	1102 West 41st Place	A227	Fail	2	0	1	3
Building 2	Holiday 101-A	1106 West 41st Place		Fail	2	0	1	3
Unit 2	Holiday 101-A	1106 West 41st Place	C122	Fail	1	0	0	1
Unit 3	Holiday 101-A	1106 West 41st Place	C124	Fail	0	0	1	1
Unit 4	Holiday 101-A	1106 West 41st Place	C224	Fail	2	0	0	2
Building 3	Holiday 101-A	1107 West 42nd Street		Fail	2	0	1	3
Unit 5	Holiday 101-A	1107 West 42nd Street	D114	Fail	1	0	0	1
Building 4	Holiday 101-A	1131 S. Bronson Ave.		Fail	6	1	2	9
Unit 6	Holiday 101-A	1131 S. Bronson Ave.	E104	Fail	1	0	0	1
Unit 7	Holiday 101-A	1131 S. Bronson Ave.	E107	Fail	4	0	0	4
Unit 8	Holiday 101-A	1131 S. Bronson Ave.	E111	Fail	1	0	0	1
Unit 9	Holiday 101-A	1131 S. Bronson Ave.	E210	Fail	2	0	0	2
Building 5	Holiday 101-A	2962 S. Francis Ave.		Fail	0	0	3	3
Unit 10	Holiday 101-A	2962 S. Francis Ave.	F106	Fail	2	0	0	2
Building 6	Holiday 101-B	106 N. Commonwealth Ave.		Fail	8	3	2	13
Unit 11	Holiday 101-B	106 N. Commonwealth Ave.	A206	Pass	0	0	0	0
Unit 12	Holiday 101-B	106 N. Commonwealth Ave.	A210	Fail	1	0	0	1
Building 7	Holiday 101-B	112 N. Commonwealth Ave.		Fail	4	2	1	7
Unit 13	Holiday 101-B	112 N. Commonwealth Ave.	B119	Pass	0	0	0	0
Unit 14	Holiday 101-B	112 N. Commonwealth Ave.	B223	Pass	0	0	0	0
Building 8	Holiday 101-B	250 S. Coronado Street		Fail	5	0	2	7
Unit 15	Holiday 101-B	250 S. Coronado Street	C106	Fail	1	0	0	1
Building 9	Holiday 101-B	258 S. Coronado Street		Fail	4	0	2	6
Unit 16	Holiday 101-B	258 S. Coronado Street	D005	Fail	2	0	0	2
Unit 17	Holiday 101-B	258 S. Coronado Street	D117	Pass	0	0	0	0
Unit 18	Holiday 101-B	258 S. Coronado Street	D215	Fail	1	0	0	1
Unit 19	Holiday 101-B	258 S. Coronado Street	D217	Fail	1	0	0	1
Unit 20	Holiday 101-B	258 S. Coronado Street	D220	Pass	0	0	0	0
Building 10	Holiday 101-B	4163 Monroe Street		Fail	1	0	1	2
Unit 21	Holiday 101-B	4163 Monroe Street	E101	Fail	1	0	0	1
Unit 22	Holiday 101-B	4163 Monroe Street	E212	Fail	1	0	1	2
Building 11	Holiday 101-C	1241 Ingraham Street		Fail	6	0	1	7
Unit 23	Holiday 101-C	1241 Ingraham Street	A202	Pass	0	0	0	0
Unit 24	Holiday 101-C	1241 Ingraham Street	A208	Fail	1	0	1	2
Unit 25	Holiday 101-C	1241 Ingraham Street	A305	Fail	1	0	0	1
Building 12	Holiday 101-C	402 S. Burlington Ave.		Fail	4	2	1	7
Unit 26	Holiday 101-C	402 S. Burlington Ave.	B102	Fail	1	1	0	2
Unit 27	Holiday 101-C	402 S. Burlington Ave.	B207	Fail	0	1	0	1
Unit 28	Holiday 101-C	402 S. Burlington Ave.	B301	Pass	0	0	0	0
Unit 29	Holiday 101-C	402 S. Burlington Ave.	B305	Fail	3	0	0	3
Building 13	Holiday 101-C	408 S. Burlington Ave.		Fail	4	0	2	6
Unit 30	Holiday 101-C	408 S. Burlington Ave.	C115	Fail	3	0	0	3
Unit 31	Holiday 101-C	408 S. Burlington Ave.	C124	Fail	1	0	1	2
Unit 32	Holiday 101-C	408 S. Burlington Ave.	C216	Fail	1	0	1	2
Unit 33	Holiday 101-C	408 S. Burlington Ave.	C217	Fail	2	0	0	2
Unit 34	Holiday 101-C	408 S. Burlington Ave.	C220	Fail	1	0	1	2
Unit 35	Holiday 101-C	408 S. Burlington Ave.	C222	Fail	2	0	1	3
Building 14	Holiday 101-C	751 S. Hoover Street		Fail	8	0	0	8
Unit 36	Holiday 101-C	751 S. Hoover Street	D203	Fail	1	0	0	1
Unit 37	Holiday 101-C	751 S. Hoover Street	D304	Fail	4	0	2	6
Unit 38	Holiday 101-C	751 S. Hoover Street	D310	Fail	3	0	2	5

Sample item	Property	Street address	Unit	Pass/fail housing quality standards	24-hour violations	10-day violations	30-day violations	Total violations
Building 15	Holiday 102	1348 W. 20th Street		Fail	3	1	0	4
Unit 38	Holiday 102	1348 W. 20th Street	B206	Fail	3	0	0	3
Building 16	Holiday 102	427 S. Union Drive		Fail	8	0	7	15
Unit 40	Holiday 102	427 S. Union Drive	D207	Fail	2	0	0	2
Unit 41	Holiday 102	427 S. Union Drive	D212	Pass	0	0	0	0
Unit 42	Holiday 102	427 S. Union Drive	D302	Fail	2	0	0	2
Unit 43	Holiday 102	427 S. Union Drive	D304	Pass	0	0	0	0
Building 17	LA Pro	1106 S. Harvard Blvd.		Fail	2	0	2	4
Unit 44	LA Pro	1106 S. Harvard Blvd.	E102	Fail	2	0	1	3
Unit 45	LA Pro	1106 S. Harvard Blvd.	E105	Fail	2	0	1	3
Building 18	LA Pro	1340 S. Westlake Ave.		Fail	4	0	1	5
Unit 46	LA Pro	1340 S. Westlake Ave.	C108	Fail	2	0	0	2
Unit 47	LA Pro	1340 S. Westlake Ave.	C202	Fail	1	0	0	1
Unit 48	LA Pro	1340 S. Westlake Ave.	C206	Fail	0	0	1	1
Building 19	LA Pro	1606 W. 47th Street		Fail	1	0	3	4
Unit 49	LA Pro	1606 W. 47th Street	F111	Fail	1	0	0	1
Building 20	LA Pro	306 S. Columbia Ave.		Fail	1	0	1	2
Unit 50	LA Pro	306 S. Columbia Ave.	B203	Fail	2	0	0	2
Unit 51	LA Pro	306 S. Columbia Ave.	B209	Fail	2	0	1	3
Building 21	LA Pro	817 S. Park View Street		Fail	3	0	1	4
Unit 52	LA Pro	817 S. Park View Street	D106	Fail	1	0	1	2
Building 22	Two Worlds	1228 S. Kingsley Drive		Fail	0	1	1	2
Unit 53	Two Worlds	1228 S. Kingsley Drive	C02	Fail	4	0	0	4
Unit 54	Two Worlds	1228 S. Kingsley Drive	C06	Fail	2	0	0	2
Building 23	Two Worlds	1401 S. Burlington Ave.		Fail	2	0	2	4
Unit 55	Two Worlds	1401 S. Burlington Ave.	F11	Pass	0	0	0	0
Building 24	Two Worlds	420 S. Union Ave.		Fail	1	0	1	2
Unit 56	Two Worlds	420 S. Union Ave.	A17	Fail	1	0	0	1
Building 25	Two Worlds	474 S. Hartford Ave.		Fail	1	1	0	2
Unit 57	Two Worlds	474 S. Hartford Ave.	B09	Fail	0	0	1	1
Unit 58	Two Worlds	474 S. Hartford Ave.	B12	Fail	3	0	1	4
Unit 59	Two Worlds	474 S. Hartford Ave.	B22	Fail	1	1	1	3
Unit 60	Two Worlds	474 S. Hartford Ave.	B24	Fail	1	0	0	1
Total:				10 pass/75 fail *	166	14	60	240

* 10 units passed, and 50 units and 25 buildings failed