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TO: Edward J. Palombizio, Director, Multifamily Division,
Pittsburgh Area Office, 3EHM

FROM: Edward F. Momorella, District Inspector General for
Audit, 3AGA

SUBJECT: Allegheny Housing Rehabilitation Corporation
Management Agent Operations
Pittsburgh, Pennsylvania

We audited the management agent operations of the Allegheny Housing Rehabilitation Corporation (AHRCO) to determine whether its management activities were administered in accordance with HUD requirements.

The report's five findings identifies that AHRCO: improperly paid employees from project funds; incurred ineligible and unsupported costs; mismanaged various aspects of the Flexible Subsidy Program; did not allocate computer costs to all entities managed and requires improvement in administering Section 8 occupancy requirements.

Report issuance was delayed because of Federal government shut downs.

Within 60 days please give us, for each recommendation in this report, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued because of the audit.

Should you or your staff have any questions, please contact Irving I. Guss, Assistant District Inspector General for Audit at (215) 656-3401.

Executive Summary

The purpose of the audit was to assess whether AHRCO complied with HUD requirements in managing its portfolio of HUD insured and subsidized projects.

AHRCO generally managed HUD insured projects as required, and projects inspected were properly maintained. Issues identified in the report indicate that AHRCO's oversight of financial and certain program areas requires improvement. From a monetary standpoint these conditions resulted in ineligible and unsupported costs of \$455,034 and \$73,486 respectively.

AHRCO employees
salaries paid by projects

AHRCO used funds from eleven HUD-insured projects to pay salaries of employees which should have been paid from the management fee. AHRCO's unfamiliarity with HUD requirements resulted in the ineligible expenditure of project funds totalling \$315,596.

AHRCO inflated the cost
of operations charged to
projects

Between January 1993 and April 1995, AHRCO inflated the cost of materials, labor and delivery fees which were charged to HUD insured projects and tenants contrary to requirements. As a result, AHRCO received \$86,096 of ineligible project funds, unsupported project funds of \$50,753, and unsupported tenant funds of \$674.

Flexible Subsidy Program
overcharged and
contracting questionable

Under the Flexible Subsidy Program, salaries for three employees were paid from both the flexible subsidy account and the project operating accounts. Also, applicable procurement procedures were not followed. As a result, the projects overpaid \$41,050 for salaries and fringe benefits and there is no assurance the rehabilitation work was performed by the lowest bidder as required.

Computer expenses
improperly allocated

AHRCO did not properly prorate expenses for computer equipment and service contracts among all projects and identity-of-interest companies which utilized the equipment as required. As a result, unsupported costs totaling \$22,059 were charged to HUD-insured projects.

Non compliance with various aspects of occupancy requirements

AHRCO's noncompliance with HUD occupancy requirements included: failure to house tenants in appropriate sized units; inadequate verification of income, assets and allowances to income; incorrect total tenant payment calculations; and failure to place tenants in order from the waiting list. Because tenants remained overhoused and were not required to pay market rent, \$12,292 in excess Housing Assistance Payments (HAP) were made.

We recommend AHRCO: (1) repay ineligible costs to the projects and excess HAP to HUD; (2) justify the eligibility of unsupported costs; and (3) comply with requirements governing management activities, procurement, and occupancy.

During our audit, the finding issues were discussed with AHRCO and where appropriate, AHRCO's comments are summarized in the findings. The draft findings were provided to AHRCO and responses received were considered in our report. AHRCO's written response and appropriate exhibits are included as Appendix B.

An exit conference was held with AHRCO on September 29, 1995.

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Abbreviations

AHRCO	Allegheny Housing Rehabilitation Corporation
CFR	Code of Federal Regulations
HAP	Housing Assistance Payments
HUD	U.S. Department of Housing and Urban Development
MIOP	Management Improvement and Operating Plan
OIG	Office of Inspector General
TTP	Total Tenant Payment

Introduction

Allegheny Housing Rehabilitation Corporation is a management agent located in Pittsburgh, Pennsylvania. An identity-of-interest exists between AHRCO, the projects managed, and companies doing business with the projects. Milton A. Washington is the Owner and a General Partner of AHRCO. Mr. Washington and AHRCO are the owners of the projects. Mr. Washington is also the President of Temple Maintenance Company and Beacon Construction Company, entities providing services for AHRCO.

AHRCO manages 12 projects which have HUD insured mortgages and/one non-insured project. These projects have 1,293 units of which 1,197 units receive HUD Section 8 subsidy payments.

Project records are maintained at the projects and at AHRCO's office at 5604 Baum Boulevard, Pittsburgh, Pennsylvania.

Audit Objective

The objective of the audit was to determine whether AHRCO managed the projects in accordance with HUD requirements. Based on survey results, the audit focused on management and other fees charged to the projects, Section 8 occupancy, procurement activities for work under the Flexible Subsidy Program, distribution of payroll expenses, and inventory costs.

Audit Scope and Methodology

We reviewed pertinent Pittsburgh Area Office and AHRCO records, and independent auditor reports. We interviewed Pittsburgh Area Office and AHRCO staff, contractors, and other persons as necessary. We performed physical inspections and tenant file reviews at four projects using a random number generator to select ten percent of the occupied units.

Audit Period

Audit work was performed between February 1995 and September 1995 and covered the period from January 1, 1994 through February 25, 1995. When appropriate, the review was extended to include other periods.

We conducted the audit in accordance with generally accepted government auditing standards.

Employees Salaries Improperly Paid From Project Funds

AHRCO used funds from eleven HUD-insured projects to pay salaries of employees which should have been paid from the management fee. AHRCO's unfamiliarity with HUD requirements resulted in the expenditure of ineligible project funds totalling \$315,596.

HUD Handbook 4381.5 REV-1, Change 3, Chapter 2, Paragraph 2-14.B. states:

"Supervisory personnel are paid from the management fee whether or not they perform supervisory or front-line tasks (e.g. if agent or agent's staff fills in for manager, agent cannot charge project for time....)"

HUD Handbook 4370.2 REV-1 for Account 6310, Office Salaries, states:

"....Front-line responsibilities include for example, taking applications, verifying income and processing maintenance requests. The account does not include salaries paid to occupancy, maintenance and regional supervisors who carry out the agent's responsibility for overseeing for supervising project operations and personnel. These salaries are paid from the management fee."

Two management officials salaries charged to projects

Between January 4, 1992 and June 2, 1995, AHRCO charged portions of the salaries for the Vice-President and the Management Development Officer to the operating accounts of eleven projects.

The Vice-President's duties included supervision of the maintenance staff and management offices as well as functioning for the manager during vacations. In addition, the Vice-President, stated housing management is a very small part of what AHRCO does. In our opinion, the functions performed by the Vice-President are supervisory and agent related and his salary is AHRCO's responsibility.

Finding 1

The Management Development Officer's duties included handling insurance for the agent, implementing safety procedures, and reviewing legal and tax matters for real estate. The duties listed are not "front-line responsibilities", they are agent responsibilities compensated by the management fee.

AHRCO staff was unfamiliar with HUD handbook requirements. The Controller said the Vice-President's salary was charged to the projects because the Vice-President fills in for the project managers when they are out. The Controller also thought the duties of the Management Development Officer qualified as "front-line" and would be eligible as project expenses.

Because the projects were charged with salaries of AHRCO personnel, eleven projects expended \$315,596 of project funds that are ineligible.

Auditee Comments

AHRCO believed "the auditors did not consider job function and responsibility" and instead focused on job titles in this finding. AHRCO again stated the duties of the Management Development Officer were front-line duties and not supervisory.

OIG Evaluation of Auditee Comments

Comparison of the employee duties with the requirements of the cited HUD handbooks was the basis of classifying the salaries as ineligible. The duties of the Management Development Officer and Vice-President were not front-line.

AHRCO's comments did not address the handbook requirements, and the ineligible costs as stated in the finding, remain in tact.

Recommendations

We recommend AHRCO:

- 1A. Repay the eleven projects the \$315,596 of ineligible costs cited through June 2, 1995 and any ineligible salaries incurred thereafter. Refrain from charging

the projects the salaries of personnel who do not perform front-line tasks.

- 1B. Implement the requirements of HUD Handbook 4381.5 REV-1 and 4370.2 REV-1.

Ineligible And Unsupported Costs Paid From HUD-Insured Project Funds

Between January 1993 and April 1995, AHRCO inflated the cost of materials, labor and delivery fees which were charged to the HUD-insured projects and tenants. The costs were inflated contrary to HUD requirements. AHRCO staff said the additional charges covered the cost of maintaining a central warehouse; overhead relating to the maintenance operation; and, disruption of the maintenance schedules. As a result, AHRCO received ineligible project funds totalling \$86,096; unsupported project funds totalling \$50,753; and unsupported tenant funds totalling \$674.

Paragraph 12(b) of the Regulatory Agreement states:

"Payment for services, supplies, or materials, shall not exceed the amount ordinarily paid for such services, supplies or materials furnished."

HUD Handbook 4381.5 REV-1, CHG 3, Chapter 2, Paragraph 2-15.A.2) states:

"If the staff work is performed out of the agent's office for several properties; ... Agents may not impose surcharges or administrative fees on top of the actual costs."

Paragraph 4b of the Management Certification requires AHRCO to:

"Exert reasonable effort to maximize project income and to take advantage of discounts and credit the project with all discounts, rebates or commissions (including any sales or property tax relief granted by the State or local government) received with respect to purchases, service contracts and other transactions made on behalf of the project."

A. Inflated material costs

Material purchases billed
20 percent above cost

AHRCO purchased materials needed for project maintenance and stored them in a central warehouse.

When the materials were used by a project or a tenant, AHRCO billed the project or the tenant the purchase price plus 20 percent. For example, AHRCO paid \$56.45 for a kitchen faucet but billed the HUD-insured projects \$71.13 for the same faucet. In another example, a tenant was billed \$233.37 for materials which cost AHRCO \$186.14.

AHRCO also purchased two sets of kitchen cabinets and related accessories at a discounted price of \$1,570. Although these cabinets and accessories were shipped directly to the project, eliminating the use of the warehouse, the project account was charged \$2,709. The difference of \$1,139 equals a mark-up of approximately 73 percent.

20 percent mark up on materials covers AHRCO's overhead

According to AHRCO's Vice-President and Controller, the 20 percent mark-up on materials was used to cover the costs AHRCO incurred in maintaining a central warehouse, i.e. utilities, tools, security, and salaries of warehouse staff. The Controller said the mark-up also covered AHRCO's cost of billing and recordkeeping.

Application of mark up is unsupported

Both the Vice-President and the Controller said charging the 20 percent warehouse fee resulted in a greater cost savings than charging the projects and tenants for the actual costs involved in maintaining the warehouse. However, the Controller admitted no analysis of the actual costs of maintaining the warehouse versus the 20 percent markup had been done. Without such documentation, there is no basis to support the validity of its 20 percent fee.

According to AHRCO's Controller, it is common practice to charge projects the original cost for large items and not pass along vendor discounts. After further discussions, the Controller said AHRCO discontinued charging both the projects and the tenants the 20 percent mark-up for materials as of June 1, 1995. Actual costs based on an approved allocation method will be charged instead.

As a result of the unjustified mark-up, and contrary to HUD requirements, the HUD-insured projects paid \$47,762 in excessive materials costs and the tenants paid \$674 in excessive materials costs. Of the total \$48,436, \$47,297 is unsupported while the remaining \$1,139 is ineligible.

B. Inflated labor costs

Excessive labor rates not justified

Between January 1993 and December 1994, AHRCO charged the HUD-insured projects labor rates of \$21.50 per hour without regard for the actual rate paid the employee or whether the employee's salary was charged to another HUD-insured project. For example, on work order 16950, AHRCO charged the Bethesda/Wilkinsburg project \$21.50 per hour for two employees. The hourly rate, including benefits, of the one employee was only \$11.06 and the salary of the second employee was routinely charged to the Bethome project. In addition, AHRCO did not use the funds received from Bethesda/Wilkinsburg to reimburse Bethome. In a few instances, the work orders did not document the maintenance person assigned to the job.

According to AHRCO's Controller, the \$21.50 per hour labor rate along with the 20 percent material mark-up were to cover AHRCO's overhead costs relating to the maintenance operation. Subsequently, the Controller said AHRCO's future plans are to charge the projects only the actual rate of the non-project employees who assist with project maintenance.

Contrary to the Regulatory Agreement, AHRCO has not justified overhead costs for its maintenance operation labor fees received from the HUD-insured projects. As a result \$81,476 charged for labor is ineligible.

C. Inflated delivery fees

Delivery costs exceed industry standards

Between January 1993 and December 1994, AHRCO charged the HUD-insured projects a delivery fee of \$25 per appliance for ranges and refrigerators. This fee was assessed whether AHRCO purchased the appliance from a vendor or moved a used one from the warehouse. Discussions with the vendors and a review of vendor invoices disclosed an average per appliance delivery cost of \$14. Also, some work orders did not adequately document the point of origin or the condition (new or used) of the appliances.

Regarding the delivery charge for new appliances, the Controller stated, the delivery fee of \$25 per appliance is

being charged since the deliveries are being made on an emergency basis. This disrupts the maintenance personnel work schedules; therefore the need for a higher billing rate. As for the delivery charges for the used appliance, the Controller was not aware this occurred.

AHRCO's Management Plan describes the duties and responsibilities of maintenance personnel as "performing maintenance service in response to resident generated work requests, scheduled preventative maintenance service and repairs originated as a result of inspection reports." The delivery and removal of appliances could reasonably be considered to be included in these duties and responsibilities.

While the Controller cited a need for the higher costs because the appliances were delivered on an emergency basis, a unit without a working range or refrigerator would fail housing quality standards. Therefore, it is the responsibility of the owner to replace the unit, at cost, no matter how disruptive it is for their work schedules.

Because AHRCO's delivery cost exceeded those of the vendor and AHRCO charged for delivery of used appliances, contrary to the Regulatory Agreement, the projects were charged ineligible costs of \$3,481. Failure to document the origin and condition of the appliances resulted in unsupported charges of \$4,130.

Auditee Comments

AHRCO submitted figures which listed warehouse expense and maintenance overhead costs totalling \$201,682 from January 1993 through April 1995. AHRCO then subtracted the unsupported and ineligible costs of \$137,523 which were reported in the finding and requested the remaining \$64,159 be reimbursed to AHRCO. AHRCO also submitted figures showing wholesale costs of eight items and the alleged savings by not buying the items wholesale.

**OIG Evaluation of
Auditee Comments**

AHRCO's response did not adequately address the recommendation which required appropriate documentation that the mark-up did not exceed the overhead necessary for

the services. For example, AHRCO did not show what the actual mark-up would equal if the amounts AHRCO is requesting are added to the materials and labor costs. Therefore AHRCO has not shown their mark-up to be less than purchasing the items wholesale. Also, the eligibility of some of the items AHRCO is including in their expense and overhead calculations, such as rent, interest on inventory, incentives paid to maintenance employees and payroll taxes on these incentives are questionable.

The actual expense and maintenance costs alleged by AHRCO have not been verified through audit.

The unsupported and ineligible costs cited in the finding remain as presented.

Recommendations

We recommend AHRCO:

- 2A. Repay the HUD-insured projects the \$1,139 of ineligible costs. Justify to HUD with appropriate documentation that the mark-up is cost beneficial to the projects and tenants, and does not exceed the overhead costs necessary for services provided. Repay the projects and tenants any portion of the \$47,297, and any mark-up charged since April 30, 1995, which cannot be justified.
- 2B. Repay the HUD-insured projects ineligible labor costs of \$81,476 and delivery fees of \$3,481 and any excess labor costs or delivery fees received since December 31, 1994. Charge the projects only the actual delivery fees and the actual salaries of the non-project maintenance employees who perform work on the projects. Repay any portion of the \$4,130 of delivery fees not adequately supported.

AHRCO Needs To Improve Its Administration Of The Flexible Subsidy Program

The following deficiencies occurred during AHRCO's administration of the Flexible Subsidy Program:

- Salaries for three employees were paid from both the flexible subsidy account and the project operating account.
- AHRCO did not follow the procurement procedures applicable to the Flexible Subsidy Program.

AHRCO staff said the deficiencies were caused by miscommunication, oversight and unfamiliarity with program requirements. As a result, AHRCO overcharged four projects \$41,050 for salaries and fringe benefits and there is no assurance work was performed by the lowest bidder, as required.

A. Employee salaries

HUD Handbook 4370.2 REV-1, Chapter 2, Paragraph 2-6.B. states:

"All disbursements from the Regular Operating Account ... must be supported by approved invoices/bills or other supporting documentation."

Salaries improperly charged to projects

AHRCO charged the project operating accounts the salaries of three employees who worked on the Flexible Subsidy Program. For example, an employee whose salary is normally charged to two projects, worked 40 hours per week for 43 weeks on the Flexible Subsidy Program. AHRCO charged each project \$10,424 for the employee's salary and fringe benefits, although such costs were payable from the Flexible Subsidy Program.

AHRCO's Controller said miscommunication caused the projects to be charged with the salaries of the employees. As a result, the projects were overcharged as follows:

B. Procurement procedures

AHRCO did not properly procure work to be performed under the Flexible Subsidy Program. AHRCO's noncompliance included the following:

- All work exceeding \$5,000 was not properly bid.
- AHRCO provided verbal work specifications and changed solicited bids through verbal negotiations.
- Work was awarded to contractors AHRCO felt were not capable of doing the entire job.

AHRCO staff cited unfamiliarity with the requirements, and the desire to give work to minority contractors as reasons for the deficiencies. As a result, there is no assurance the work was procured at the lowest price; the work will be performed satisfactorily; and favoritism was not a factor in awarding contracts.

1. Work not bid

Section 10 of the Financial Assistance Contract states:

"The Housing Owner shall solicit written cost estimates (i.e. bids) from at least three contractors or suppliers for any work item which the Housing Owner and the Commissioner estimate will cost \$5,000 or more."

AHRCO did not solicit bids for the following:

Work Item

Amount

Identity of interest companies received benefit of non-bid work

The demolition work was added to the contract between AHRCO and Beacon Construction Company. Beacon Construction Company has an identity-of-interest with AHRCO. The flue relining and register replacement were added to the contract between Beacon Construction Company and Temple Maintenance Company. Temple Maintenance also has an identity-of-interest with AHRCO.

According to the Management Development Officer, not bidding the demolition work was an oversight. However, AHRCO did the demolition so the other rehabilitation work could be done. The additional flue work was not added to the bid because AHRCO did not think of it. The register replacement was not bid because the money became available after the original work was bid. Since Temple Maintenance was already putting in the furnaces, the register replacement work was just added to their contract.

2. Verbal changes to specifications and bids

The Specifications for Alterations to Mon View Heights, Information for Bidders, Paragraph 9 states:

"No interpretation of the meaning of the plans, specifications or other pre-bid documents will be made to any bidder orally.

"Any and all such interpretations and any supplemental instructions will be in the form of written addenda to the specifications ..."

Although the lead based paint abatement was included in the Management Improvement and Operating Plan (MIOP)

submitted to HUD, the item was not included in the detailed specifications. The Construction Manager for Beacon Construction explained to each bidder what was needed for the lead based paint encapsulation work.

AHRCO received the following bids for lead based paint encapsulation work:

Verbal contract changes caused cost to exceed low bid

Through verbal negotiations with Contractor A, AHRCO added a second coat of paint and the use of a more expensive encapsulation for lead based paint to the contractor's bid. These changes made the bid price of Contractor A equal to the bid price of Contractor B. AHRCO then split the work between the two contractors. When writing the contracts, AHRCO increased the scope of work to include additional cleaning and interior painting. Exterior painting was also added but at no specified cost. These changes brought the base contract amount to \$399,350. This exceeded the \$374,900 bid of Contractor C which included the cleaning that was added to the other contracts.

AHRCO's Management Development Officer was not familiar with the requirements of the Addenda and Interpretations stated in the specifications, and resulted in the improper splitting and increased cost of the work.

3. Responsible bidders

Section 10 of the Financial Assistance Contract states:

"The Housing Owner agrees to accept the bid which represents the lowest price taking into consideration the bidder's reputation for quality or workmanship or materials, timely performance ..."

AHRCO split the work described in the previous subsection of the finding between Contractor A and Contractor B because they did not feel either was capable of doing the work for all of the units involved.

AHRCO said the contractors were small and they liked to give work to minority contractors. Contractor A was a minority contractor.

By not bidding all work exceeding \$5,000 and awarding the work which was bid to responsible bidders, AHRCO cannot assure the work was procured at the lowest price and that favoritism was not a factor in selecting the contractors.

* * * *

AHRCO charged both the flexible subsidy account and the project operating accounts for employees who performed work under the Flexible Subsidy Program, and did not follow the procurement procedures applicable to the Flexible Subsidy Program. Miscommunication, oversight and unfamiliarity with program requirements led to these deficiencies according to AHRCO staff. As a result, AHRCO overcharged four projects \$41,050 for salaries and fringe benefits and there is no assurance work was performed by the lowest responsible bidder, as required.

Auditee Comments

AHRCO agreed to repay the four projects \$40,450 for payroll distribution due to an administrative error conditioned upon the OIG agreeing the amount be offset against the amount AHRCO states they are due from Finding 2. AHRCO subtracted \$600 for an employee which AHRCO said did not work the week of December 31, 1994.

AHRCO agreed with the two remaining recommendations for this finding.

OIG Evaluation of
Auditee Comments

The amount cited in this finding did not include any amount for the cited employee for the week ending December 31,

Finding 3

1994. Further, the ineligible \$41,050 is not impacted by Finding 2 and repayment to the projects is necessary.

Recommendations

We recommend AHRCO:

- 3A. Repay the four projects the \$41,050 and any duplicate employee salaries paid after the payroll ending June 2, 1995.

We recommend your staff verify AHRCO:

- 3B. Solicit bids from at least three independent contractors to ensure costs charged by the identity-of-interest firms under part B1 were the lowest. Repay the flexible subsidy account any amount which exceeds the lowest solicited bid.
- 3C. Assure staff is aware of and follows applicable bidding and contract requirements.

AHRCO Did Not Properly Prorate Computer Expenses

AHRCO did not properly prorate expenses for computer equipment and service contracts among all projects and identity-of-interest companies which utilized the equipment as required. According to AHRCO's Controller the costs were allocated to the HUD-insured projects because they generate most of the computer work. As a result, unsupported costs totaling \$22,059 were charged to HUD-insured projects.

According to HUD Handbook 4381.5 REV-1, CHG 3, Chapter 2, Section II, Paragraph 2-15.A.2a:

"If the staff work is performed out of the agent's office for several properties; a. prorate the associated costs among the projects served in proportion to actual use: ... actual office expenses, fees and contract costs directly attributed to the front-line duties."

Section II, Figure 2-4 illustrates as an example of funds paid from the project account:

"... costs allowed by HUD for prorated share of centralized, computer accounting systems ..."

Computer costs not allocated to all projects and companies

AHRCO charged all costs related to a purchase of computer equipment and maintenance service contracts to the HUD-insured projects only. These costs were allocated to the HUD-insured projects on a straight line method even though the number of units in the HUD-insured projects ranged from 38 to 326. Two identity-of-interest companies and a 115-unit project which received HUD Section 8 subsidy but was not HUD-insured, utilized the equipment, but were not allocated any of the costs.

According to the AHRCO's Vice-President, tenant certifications/recertifications, vacancy and damage reports

for the non HUD-insured project are computerized. The Controller stated the costs were charged to the HUD-insured projects only because they generate most of the computer workload. The straight line basis was used because it was easy to calculate. The Controller stated the computers are utilized by data entry staff responsible for entering information relating to the HUD projects.

By not following HUD requirements for allocating project expenses, AHRCO improperly allocated costs totalling \$22,059, for computer equipment and maintenance contracts; to the HUD-insured projects.

The draft finding included unsupported costs of \$130,986 for administrative/computer fees. Based on AHRCO's written response and information provided by the Pittsburgh Area Office, this portion of the draft finding was removed from the final report.

Auditee Comments

AHRCO did "not concur with the guideline provided by ... Handbook 4381.5 REV-2." saying the Handbook is "designed to serve as a reference for ... Management Agents." AHRCO said the Handbook "provides basic guidance regarding ... agent responsibilities and HUD procedures and is not regulation." AHRCO agreed a portion of the computer costs should have been allocated to all users of the equipment but proposed "no prior allocation be made". AHRCO said, while they disagreed with the per-unit cost allocation, they would accept either the per-unit or straight line allocation method for future use.

OIG Evaluation of
Auditee Comments

AHRCO's comments failed to recognize the requirement of Paragraph 2.a. of the Management Certification which states they agree to comply with the project's "Regulatory Agreement, Mortgage and Mortgage Note, any Subsidy Contract or Workout/Modification Agreement, and any applicable HUD Handbooks, notices or other policy directives that relate to the management of the project." Therefore, reallocation of the computer costs based on the per-unit method is necessary.

Recommendation

We recommend AHRCO:

- 4A. Provide HUD the cost allocation to prorate the \$22,059 of unsupported computer costs to all managed projects and entities. Repay the HUD-insured projects for improper assessments covering the period January 1992 to date.

AHRCO Needs To Improve Compliance With Occupancy Requirements

A sample of thirty-six tenant files at four projects disclosed non-compliance with HUD requirements in the following areas:

- Tenants were housed in inappropriately sized units.
- Income and assets were not adequately verified.
- Allowances to gross income were not verified.
- Total tenant payment calculations were incorrect.
- Tenants were not selected from waiting lists.

AHRCO's noncompliance with requirements resulted in a lack of assurance the Total Tenant Payment (TTP) and Housing Assistance Payments were correct and that all applicants were treated fairly. Because tenants remained overhoused and were not required to pay market rent, \$12,292 in excess Housing Assistance Payments were made.

A. Unit size inappropriate

AHRCO's Resident Selection Criteria states under unit size standards:

"In order to avoid overcrowding and make the best use of available space and subsidy, (AHRCO) has designated unit size standards that conform with state and local laws as follows:

<i>Efficiency</i>	<i>1 Occupant</i>
<i>1 Bedroom Apartment</i>	<i>1 to 2 Occupants</i>
<i>2 Bedroom Apartment</i>	<i>2 to 4 Occupants</i>
<i>3 Bedroom Apartment</i>	<i>3 to 6 Occupants</i>

Those properties with 4, 5 or 6 bedrooms will increase the number of occupants accordingly."

According to number five of AHRCO's eligibility criteria:

"... When an appropriate size unit becomes available, a transfer can be required with proper notice."

The Residential Lease between AHRCO and tenants under Section 19 - Size of Dwelling states:

"The Tenant understands that HUD requires the Landlord to assign units according to the household and the age and sex of the household members. If the Tenant is or becomes eligible for a different size unit and the required size becomes available, the Tenant agrees to: a. Move within thirty (30) days after the Landlord notifies him/her that a unit of the required size is available within the project; or b. Remain in the same unit and pay the HUD approved market rent."

24 CFR Section 886:325(c) states:

"If the owner fails to offer the family a unit appropriate for the size of the family when such unit becomes vacant and ready for occupancy, HUD may abate housing assistance payments to the owner for the unit occupied by the family...."

Sample identified five tenants overhoused

In addition to the 36 files selected for review, a tenant recertification provided by the Pittsburgh Area Office was included in the review for this area. Five of the 37 tenants reviewed resided in units which were too large based on family size.

For example, the tenant file showed one person living in a four bedroom unit from at least June 1, 1987 through the recertification effective June 1, 1994. In a letter dated October 25, 1990, the Pittsburgh Area Office instructed AHRCO to move the tenant into "an appropriate sized unit or adjust the contract rent to an amount comparable to a

one-bedroom unit". AHRCO wrote a letter to the tenant dated February 8, 1991 requiring a transfer to a one-bedroom unit or demanding market rent effective April 1, 1991. According to the most recent recertification effective June 1, 1994, the tenant remained in the four-bedroom unit and did not pay market rent.

Although only five of the 37 tenants from our sample were overhoused, the MIOP showed 63 families at one project were not residing in units matching their household needs.

Two project managers believed tenants were no longer transferred because of the expense of preparing two units instead of one but deferred to the Vice-President for an explanation. The Vice-President provided several reasons tenants may not be transferred. These were:

- AHRCO had been unsuccessful in enforcing the lease which requires the tenant to pay market rent if they do not transfer when requested. Because of their past experience of losing before the magistrate, the matter of transferring tenants has not been pursued. The Vice-President provided no evidence to support tenants were ever taken before a magistrate or judge.
- It is not realistic to require tenants to move to smaller sized units after they have lived in the same unit for many years.
- It is AHRCO's policy not to transfer tenants who are delinquent because the tenant would receive a 30-day notice to vacate. It would not make sense to transfer a tenant you were trying to evict.
- An agreement with the Pittsburgh Area Office allowed AHRCO to keep tenants at one project in their units in order to keep the project integrated. The Pittsburgh Area Office stated it would be a Fair Housing & Equal Opportunity violation if tenants were allowed to live in units of a certain size to achieve a racial mix at the project.

While the Vice-President stated a tenant who was delinquent would not be transferred because AHRCO would try to evict them, the file review showed the history of delinquent rent and 30-day notices could continue for years. In the case cited above, the tenant received seven 30-day notices dating back to at least April 25, 1988. As of the recertification effective June 1, 1994, the tenant had not been evicted. By using delinquency of rent as a criteria for not transferring tenants, AHRCO is, in effect, rewarding overhoused tenants for being delinquent by not transferring them into smaller, appropriately sized units.

AHRCO agreed in the MIOP to transfer tenants at the project receiving flexible subsidy funds. The MIOP does not exclude transferring tenants with delinquent rent or 30-day notices. This gives the appearance AHRCO will only transfer tenants when additional HUD funding is dependent upon such transfers.

By not requiring tenants to move into the proper size units or pay market rent, HUD paid assistance for five tenants of at least \$12,292 which was excessive. In addition, HUD subsidy was not efficiently used because AHRCO did not house as many families as it could.

B. Income and asset verification

HUD Handbook 4350.3 CHG-1, Chapter 3 states:

Section 1, Paragraph 3-1.b.(1): "Net family assets DO include cash in savings and checking accounts ...".

Section 3, Paragraph 3-17.a.: "Owners must verify all income, expenses, assets, household characteristics and circumstances that affect eligibility or tenant rent."

Section 3, paragraph 3-19.a.(3): "When written verification is not possible, the next most acceptable form is direct contact with the source, in person or by telephone. The owner must document the conversation in the applicant's file including all information that would have been included in a written verification."

Inadequate verification of five tenants income and assets

AHRCO either did not verify or did not adequately verify income and assets for five tenants. For example, a telephone verification included in a tenant file had only the monthly assistance payment. It did not include the date and time the information was verified; the name of the AHRCO employee who placed the call, or the name of the person at the Department of Public Assistance who verified the information. In addition, AHRCO did not verify income for an adult member of the household. Project managers attributed these deficiencies to staff oversight, delays in obtaining information from public assistance agencies, and failure of a tenant to provide documentation. Without proper verification, there is no assurance the proper assistance has been calculated.

C. Allowances to income

HUD Handbook 4350.3 CHG-1, Chapter 3, Section 3, Paragraph 3-17.a. states:

"Owners must verify all income, expenses, assets, household characteristics and circumstances that affect eligibility or tenant rent."

HUD Handbook 4350.3 CHG-5, Chapter 3, Exhibit 3-2, Paragraph T.2. states:

"For handicapped head or spouse -- evidence of receipt of Supplemental Security Income for the disabled, handicapped or blind or Social Security disability benefits. If none of these benefits is received, a physician's certificate is required."

HUD Handbook 4350.3 CHG-4, Chapter 3, Exhibit 3-2, Paragraph P.2.states:

"Verifications must specify the hours and days during which the care is provided, the names of the children cared for, and the frequency and amount of compensation received...."

Income allowances for four tenants inadequately verified

AHRCO did not verify allowances adjusting gross income for four tenants. One tenant was allowed a handicap/disability allowance of \$400 annually when the handicap/disability was not verified. For two other tenants, expenses for child care were not adequately verified because the hours and days the care was provided were not specified on the verifications. For the remaining tenant, AHRCO's written response to the report stated three children were living in the unit. The tenant did not receive an allowance for dependent children as required.

An assistant project manager thought the disability pension from the Veteran's Administration was sufficient to verify the handicap/disability. The Vice-President said HUD Handbook 4350.3, Chg. 24, Chapter 2, Paragraph 2-26d prevented AHRCO from asking the tenant about their handicap. This paragraph, however refers to applicants--not in-place tenants. The Vice-President provided written comments saying "Verification of disability has been requested from the Veteran's Administration. Because AHRCO's response did not include verifying handicap/disability status as required, the potential exists for ineligible tenants to be placed in housing and to improperly receive handicap/disability allowances.

A project manager was unaware of the HUD Handbook requirements for verifying child care expenses. Without adequate verification for allowances, there is no assurance the proper assistance for the cited tenants was paid.

D. Incorrect total tenant payment

HUD Handbook 4350.3, CHG-1, Exhibit 3-1 Part A, Paragraphs 2.a. and 2.b. state annual income includes:

"The gross amount (before deductions for medicare, etc.) of periodic social security payments...."

"Annuities, insurance policies, retirement funds, pensions, disability or death benefits and other similar types of periodic receipts."

Paragraphs 3-6. regarding alimony and child support states:

"Count the amount specified in a divorce settlement or separation agreement unless the applicant: a. certifies the income is not being provided; and b. has made reasonable efforts to collect the amount due, including filing with courts or agencies responsible for enforcing payments."

Improper rent calculations

AHRCO did not properly calculate rent for five tenants at three projects. Rents were not based on the total income for these tenants. For example, a verification showed a tenant received public assistance of \$403 per month and court-ordered child support of \$50 per month. When determining TTP, AHRCO did not include the child support amount. As a result, the HAP was overstated by \$15 per month.

AHRCO staff said some amounts were not included in the TTP calculations because they were not certain the tenants received the income. Other errors in HAP calculations were attributed to oversight.

As a result, the HAP for cited tenants was overstated. AHRCO provided revised recertifications for two tenants retroactively correcting the HAP.

E. Tenant admissions

AHRCO's Resident Selection Criteria, Applications and Screening-Procedures states:

"... If the applicant appears to meet the criteria for eligibility in (this) community, the application will be placed on a waiting list in the order of the date and time received, according to unit size and program requirements."

HUD Handbook 4350.3 CHG-24, Chapter 2, Paragraph 2-29.b. states:

Improper use and control
of waiting lists

"The owner's records should indicate the date and time the applicant is placed on the waiting list."

A review of 23 tenants at three projects disclosed 15 placed into units were not on the waiting list. A review was not performed at the fourth project because no prior waiting list was available. In addition, the time of day the applications were submitted was not included on the lists.

AHRCO stated some were prior tenants and household members of existing tenant households which were transferred to other units. No explanation was provided for tenants who were placed but did not fit into either preceding category. Also, AHRCO provided no explanation for not including time of application on the waiting list but said the time will be included in the future.

Because AHRCO placed applicants who were not on the waiting list into units, there is no assurance all applicants were considered fairly when housing tenants.

In summary, AHRCO's noncompliance with requirements resulted in a lack of assurance the Total Tenant Payment and Housing Assistance Payments were correct and that all applicants were treated fairly. Because tenants remained overhoused and were not required to pay market rent, \$12,292 in excess Housing Assistance Payments were made.

Details for the deficiencies cited in the finding's five sections were provided to AHRCO.

Auditee Comments

AHRCO did not concur with the finding and felt appropriate investigation by the auditors would have eliminated the need for most of the comments.

Regarding the example used for inappropriate unit size, AHRCO said the tenant received a court order granting the tenant custody of her grandchildren in April 1994. AHRCO also submitted documentation showing the tenant received monthly income for foster care of the grandchildren.

AHRCO stated the comments made by the Vice-President regarding transferring tenants were either not made or were taken out of context. AHRCO stated they "routinely transferred residents that met the transfer requirements" and stated 115 transfers had been made since 1990.

Regarding verifying income, assets and allowances to income, AHRCO stated the staff had been instructed to follow proper procedures or was given additional training on the proper procedures.

AHRCO said some applicants may have been left off of the updated waiting lists in error. However, "the management staff has been instructed to insure that all applicants appear on the waiting list until they are housed." AHRCO also stated tenants may not appear on the waiting list because they occasionally provide housing for families in various witness protection programs.

OIG Evaluation of Auditee Comments

On several occasions AHRCO was asked to provide documentation of the items cited in the findings. AHRCO failed to provide the information. For instance, at no time during the audit was documentation provided to show more than one person residing in the four-bedroom unit. The recertifications in the file show only one tenant and do not include the income received for the children. The recertifications also do not give the tenant an allowance for dependent children. In addition, the waiting list provided with the documentation was not the waiting list provided during the audit. Documentation provided to support the auditee comments only proved to support the need for better verification procedures and resulted in an increase in the number of cases where: (1) income and assets were not properly verified; (2) allowances to income were not properly verified; and, (3) Total Tenant Payment was not properly calculated.

Although AHRCO stated a tenant received custody of their grandchildren in April 1994, documents submitted by AHRCO show the tenant received custody of one grandchild in February 1994. Therefore, the excessive

subsidy paid for the tenant from February 1994 through June 1995 was deleted from the total excessive Housing Assistance Payments. This reduced the ineligible amount from \$16,406 to \$12,292.

All comments in the report which were attributed to AHRCO staff were made by AHRCO staff and were presented in context.

Analysis of the documents submitted by AHRCO showed only 89 transfers completed since 1990. Of the 89 completed transfers, only 21 appear to have been completed in order to correct over-or under-housing conditions. The remaining 68 transfers were same-size unit transfers (one-bedroom to one-bedroom, two-bedroom to two-bedroom, etc.) and/or were completed at Mon View Heights where transfers were required by the Flexible Subsidy Contract.

At no time during the audit did AHRCO state a tenant was placed into a unit as a result of a witness protection program.

Recommendations

We recommend AHRCO:

- 5A. Repay HUD \$12,292 for excess HAP received for the overhoused tenants.
- 5B. Transfer all over and underhoused tenants according to HUD requirements and the residential lease. Verify all income and allowances adjusting income for tenants cited and adjust rent as necessary from the most recent certification or recertification. Recertify tenants, if necessary, and adjust HAP retroactively for the most recent certifications as cited.
- 5C. Establish a system to ensure waiting lists are maintained in order of date and time of application and applicants are properly selected from the list. Maintain documentation to support applicants are properly selected.

We recommend your staff:

- 5D. Abate rents for the cited overhoused tenants and any additional tenants which remain over or underhoused due to AHRCO's failure to transfer them when the correct unit size becomes available.

Internal Controls

In planning and performing our audit, we considered internal control systems of the management of the Allegheny Housing Rehabilitation Corporation to determine our auditing procedures and not to provide assurance on internal controls. Internal control is the process by which an entity obtains reasonable assurance as to achievement of specific objectives. Internal control consists of interrelated components, including integrity, ethical values, competence, and the control environment which includes establishing objectives, risk assessment, information systems, control procedures, communication, managing change, and monitoring.

Internal controls assessed

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

- Management fees
- Occupancy requirements
- Payroll distribution
- Procurement activities
- Project maintenance costs

We evaluated all of the relevant control categories identified above, by determining the risk exposure and assessing control design and implementation.

Significant weaknesses found

A significant weakness exists if internal control does not give reasonable assurance that the entity's goals and objectives are met; that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss and misuse; and that reliable data are obtained, maintained and fairly disclosed in reports. Based on our review, we believe the following items are significant weaknesses in AHRCO's operations:

- Occupancy requirements
- Payroll distribution
- Procurement activities
- Project maintenance costs

These weaknesses are detailed in the findings in this report.

Follow Up On Prior Audits

All prior audit findings have been resolved.

Schedule Of Ineligible And Unsupported Costs

<u>Finding Number</u>	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>
1	\$315,596	\$51,427
2	86,096	
3	41,050	
4		22,059
5	<u>12,292</u>	
	<u>\$455,034</u>	<u>\$73,486</u>

- 1/ Ineligible costs are not allowed by law, contract, HUD or local agency policies or regulations.
- 2/ Unsupported costs are not clearly eligible or ineligible but warrant being contested because of the lack of documentation supporting the need to incur such costs.

Auditee Comments

Please note that AHRCO's response is in draft finding order. Report finding presentation has been changed as follows:

<u>Draft Finding</u>	<u>Report Finding</u>
1	4
2	5
3	1
4	2
5	3

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