audit report

OFFICE OF INSPECTOR GENERAL

Issue Date	October 16, 1995
Audit Case Number	96-AT-203-1001

TO: Ledford Austin, Director, Office of Public Housing, Greensboro, North Carolina, 4FPH

FROM: Kathryn Kuhl-Inclan
District Inspector General for Audit-Southeast/Caribbean, 4AGA

SUBJECT: Pender County Housing Authority
Section 8 Program
Burgaw, North Carolina

We have completed an audit of the books and records of the Pender County Housing Authority pertaining to its Section 8 Housing Program for the period July 1, 1992, through April 30, 1995. Our objective was to determine if the Authority used Section 8 Program funds for eligible purposes.

We reviewed the Authority's system of internal controls over cash disbursements for administrative costs. We reviewed 100 disbursements totaling $40,564 made by the Authority in payment of administrative costs for eligibility and support. We examined the list of Section 8 unit owners for evidence of conflict of interest.

Our audit was performed in June 1995 in accordance with generally accepted government auditing standards.

Within 60 days please give us a status report for each recommendation 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.

We have provided a copy of this report to the auditee.

We appreciate your cooperation during the audit. Should you or your staff have any questions, please contact Nancy H. Cooper, Assistant District Inspector General for Audit, at (404) 331-3369 or Bruce Milligan, Senior Auditor, at extension 4056.

SUMMARY

Our tests showed that the payments made for administrative costs were for eligible costs. However, the Authority's administrative expenses exceeded its income for the past several years. The Authority had a cumulative operating deficit of $35,331 and was able to continue operations only because it: (1) borrowed $13,100 from a bank, and (2) did not pay $17,385 it owed to HUD. The operating losses were caused by ineffective budgeting, improper allocation of costs, and loss of potential income. These management problems jeopardize the Authority's ability to continue its Section 8 Program. In addition, the Authority permitted a member of the Board of Commissioners to have two units in the Section 8 Program in violation of the Annual Contributions Contract (ACC). This represented a conflict of interest.

We discussed the results of our audit with the Authority Director on July 18, 1995. The Director generally agreed with the findings and chose not to submit written comments.

BACKGROUND

The Authority had a Section 8 Program of 214 authorized units under ACC No. A-3569. In addition, the Authority owned and managed eight Farmers Home Administration (FmHA) housing units.

The Authority earned administrative fees of $138,304 during fiscal years 1993 and 1994. However, the Authority incurred administrative expenses of $157,973 for the same period which resulted in a deficit of $19,669.

FINDINGS AND RECOMMENDATIONS

1 - Income and Expenses Not Properly Controlled

The Authority's administrative expenses exceeded its income for the past several years. The Authority had a cumulative operating deficit of $35,331 and was able to continue operations only because it borrowed $13,100 from a bank and had not repaid $17,385 it owed to HUD. The operating losses were caused by ineffective budgeting, improper allocation of costs, and loss of potential income. These management problems jeopardize the Authority's ability to continue its Section 8 Program.

The ACC, Part II, Section 201, states that the Authority shall at all times operate each project in an efficient and economical manner. Office of Management and Budget Circular A-87, Cost Principles for State and Local Governments, Attachment A, Section C.2, provides that a cost is allocable to a particular cost objective to the extent of benefits received by such objective.

For each of the 3 years in our audit period, the Authority's operating expenses exceeded its operating income. The operating losses by year were:

Year Ended	Loss
6/30/92	$ 6,505
6/30/93	13,784
6/30/94	8,417

At June 30, 1994, the Authority's cumulative losses from these 3 years and previous years was $35,331. The Authority anticipated an additional loss of about $8,500 for the year to end June 30, 1995.

The Authority was able to keep operating only because: (1) it had an unsecured loan of $13,100 from a bank, and (2) it had received excess funding of $17,385 from HUD which the Authority had not repaid.

We identified three conditions which contributed to the Authority's operating losses.

- When we performed our review in June 1995, the Authority had all of its authorized Section 8 units under lease. However, in fiscal years 1993 and 1994, the Authority lost about $15,000 in income from administrative fees because it had from 13 to 29 authorized Section 8 units which were not under lease.

- The Authority charged all of its administrative costs to the HUD Section 8 Program although the Authority also owned and administered a small FmHA housing project. We estimated the Authority should have charged about $3,000 of its administrative costs annually to the FmHA project. At June 30, 1994, the date of the Authority's last annual audited financial statements, the Authority had accumulated retained earnings of $31,218 for its FmHA project. Thus, the FmHA project had generated excess funds in past years which the Authority could have used to reimburse the Section 8 Program for excessive allocations of the Authority's administrative costs. At June 30, 1994, the FmHA project had excess cash of only about $7,000.

- The Authority did not prepare realistic and effective operating budgets. For example, the budgets showed only combined amounts for the Section 8 and FmHA projects with the result that each program could not be evaluated separately. Also, the budget expense categories did not match the cost accounts in the Authority's accounting system. Finally, the Authority overestimated Section 8 Program income by about $31,000 for fiscal year 1995.

The Authority had made some modest reductions in administrative costs. However, a combination of larger cost savings and increased income was needed to balance expenses with income and repay the Authority's debts. The Authority's ability to operate the Section 8 Program is jeopardized until it solves its financial problems.

Authority Comments

The Director generally agreed with the finding and stated that in the future the Authority would propose to FmHA to allocate some of its administrative costs to the FmHA project.

Recommendations

We recommend that you require the Authority to:

1A. Reimburse the Section 8 Program from the FmHA Program for an equitable share of the Authority's past administrative costs which have been paid entirely by the Section 8 Program.

1B. Repay the $17,385 owed to HUD.

1C. Establish financial control over the Section 8 Program to prevent future operating deficits. These controls should provide for a combination of additional income resources, expense cuts, and effective budget procedures. If the Authority cannot establish sufficient control to prevent future operating deficits, we recommend the Section 8 Program be transferred to another agency.

2 - Conflict of Interest by a Member of the Board

The Authority permitted a member of its Board of Commissioners to have two units in the Section 8 Program in violation of the ACC. This represented a conflict of interest.

The ACC, Part II, Section 2.13, prohibits the Authority from entering into a contract in connection with the program in which any employee or board member has an interest unless a waiver is obtained from HUD.

A new member was appointed to the Authority's Board of Commissioners on March 7, 1994. At that time the board member owned two units in the Authority's Section 8 Program. One of the units had been in the program since May 1979 and the other since December 1990. One of the units was dropped from the program in April 1995, but the unit was scheduled to again be included in the program after inspection by the Authority.

The Authority's Executive Director did not believe there was a conflict of interest based on a State law which permitted a board member to receive payments as long as the member did not vote on matters affecting the member's own property. However, HUD's requirements do not include such an exception.

We did not identify any adverse effect from the board member's ownership of the units in the program. To prevent any actual or perceived conflict of interest, the Authority should obtain HUD approval for keeping the board member's units in the program.

Authority Comments

The Authority Director agreed with the finding.

Recommendation

2A. We recommend that you determine if the Authority may keep the board member's units in the program. If the units are to be retained, we recommend you require the Authority to implement procedures to prevent any conflict of interest.

INTERNAL CONTROL

In planning and performing our audit, we considered the internal control systems of the Pender County Housing Authority to determine our auditing procedures and not to provide assurance on internal control. Internal control is the process by which an entity obtains reasonable assurance as to the achievement of specified 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.

A significant weakness exists if internal control does not give reasonable assurance that the entity's goals and objectives are met; that resources 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 concluded that weaknesses existed in the Authority's procedures for allocating administrative costs to its programs and in its budgeting. The weaknesses are discussed in finding number 1.

SCHEDULE OF INELIGIBLE COSTS

Recommendation	Ineligible Costs[1]
1A	$ 3,000[2]
1B	17,385
Total	$ 20,385

[1] Ineligible amounts obviously violate law, contract, HUD or local agency policies or regulations.

[2] Approximate annual amount.

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