



**U.S. Department of Housing and Urban
Development**
New England Office of District Inspector General
for Audit, 1AGA
Thomas P. O'Neill, Jr. Federal Building
Room 370
10 Causeway Street
Boston, Massachusetts 02222-1092
Audit Related Memorandum
99-BO-199-0802

September 30, 1999

MEMORANDUM FOR: Donald J. LaVoy, Acting Director, Real Estate Assessment
Center, X

FROM: William D. Hartnett, District Inspector General, Office of Audit, 1AGA

SUBJECT: Implementation of the Real Estate Assessment
Center's Physical Inspection Assessments

INTRODUCTION

The purpose of our review was to assess the implementation of the Real Estate Assessment Center's (REAC) operations pertaining to physical inspection assessments. REAC provides assessments to help HUD monitor the properties in its public housing, subsidized housing and insured housing portfolios.

REAC has contracted with private companies to review up to 45,000 projects in HUD's portfolios. As of May 3, 1999 11,600 inspections were performed. Through the standardization of treatment for all properties in the assisted and insured portfolios, the physical inspection assessment subsystem has the potential to be a useful tool for informed decision making on a national basis.

We have identified two unresolved concerns and made three recommendations to strengthen REAC's implementation process. The recommendations will be controlled in the Departmental Automated Audits Management System. Within 30 days for each recommendation, please advise us on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why the action is not considered necessary. Also, please furnish us with copies of any correspondence or directives issued.

Should you or your staff have any questions, please contact Stephen D. King, Assistant District Inspector General at 617-565-5259.

SUMMARY

The purpose of our review was to evaluate the implementation of the physical inspection assessments by the Real Estate Assessment Center (REAC). Created in 1997 as part of the HUD 2020 Management Reform, REAC will evaluate the condition of public and assisted housing and the performance of public housing agencies and other assisted property owners. REAC is developing seven distinct assessments which are estimated to be fully operational no earlier than March 31, 2000. Initially, the 2020 Reform had REAC working on four assessments—physical inspections, financial assessments, management assessments and resident satisfaction surveys. As the initial concept evolved, HUD realized that the systems being developed at REAC could be applied, with some modifications, to other aspects of its business. HUD is making a significant commitment in developing REAC. HUD has budgeted over \$62.9 million to develop all of the assessments and operate REAC.

REAC's Physical Inspection Assessment Subsystem was built through: (1) developing criteria to identify potential deficiencies in each inspectable item and assigning numeric values to deficiencies, (2) hiring contractors to use these criteria to inspect properties and (3) evaluating the results of the contractor's observations. Inspections are paid out of the appropriations supporting the creation of the projects and not out of funds for developing the assessments and operating REAC. REAC has entered into six contracts under these two procurements and could spend up to \$117.4 million for inspections under these contracts.

REAC maintains two groups of professional inspectors—the physical assessment standards team and the quality assurance inspection team—to maintain consistent quality of the contractors' inspections. These in-house inspectors verify the quality of REAC's contractors, improve the quality of training, and revise the inspection methodology, where necessary.

While results of inspections have shown that a majority of properties are in fairly good condition, HUD needs assurance that concerns identified in its inspections are corrected. We are concerned that a means of tracking findings and issues developed from the inspections has not been implemented.

Although REAC hires contractors to perform the physical inspections of properties, the monitoring of these properties continues to be the responsibility of other divisions within HUD—the Office of Public and Indian Housing and the Office of Housing. REAC and the Office of Public and Indian Housing have defined their relationship in a protocol. While a draft protocol exists, the relationship between REAC and the Office of Housing is still being defined.

HUD has not determined that the benefits derived from the physical inspection assessment subsystem are commensurate with the cost of the subsystem. The baseline being established by REAC gives HUD the opportunity to evaluate the needs of its portfolio against the resources available. To take full advantage of this opportunity, HUD needs to know the cost of the

inspection assessment system in order to compare the cost with the benefits and the available resources.

REAC has developed and is implementing a physical assessment process that should help HUD to monitor its Public and Indian Housing and Multifamily property portfolios. While the process of scoring inspections is far along in development, actual implementation and use of this process for monitoring may be more than a year away. Adequate coordination between REAC and the program offices is essential to realizing the expected benefits of the inspection assessments. While we believe that this system has the potential to be a useful tool for informed decision making, we believe that our concerns about the quality assurance reviews, the tracking of issues developed from inspections and the lack of a cost benefit analysis need to be addressed for successful implementation of the physical inspection assessment process.

The Office of Public and Indian Housing and the Office of Housing have undergone substantial downsizing as a result of the HUD 2020 management reform. A major question that still needs to be answered will be whether the Program offices will have sufficient resources to address the assessments being performed by REAC. Without adequate resources to carry out this function, the intended benefits will not be realized. We are starting a separate review which will assess the usage of the information provided by REAC.

On August 30, 1999, we provided REAC with a copy of the draft report for comment. We received REAC's response on September 21, 1999. REAC is already initiating action for two of the four recommendations. Based upon their response, one recommendation was revised and the remaining issue was considered resolved. We have included pertinent comments in the Findings section of the report. REAC's response is included in its entirety in Appendix B.

BACKGROUND

The Real Estate Assessment Center (REAC) is a new national management center within HUD established to centralize and standardize the way the Department evaluates the condition of over 3,000 public housing authorities with roughly 15,000 properties and over 30,000 properties insured by the Federal Housing Administration and/or receiving project-based subsidy under the Section 8 program. REAC is designed to give the Department a more comprehensive and consistent vehicle for portfolio oversight and for prioritizing and directing its resources to public housing authorities and multifamily properties.

Responsibility for overseeing the individual public housing authorities and multifamily properties continues to belong to the Office of Public and Indian Housing and the Office of Housing, respectively. REAC only performs assessments and does not resolve any project issues arising from those assessments.

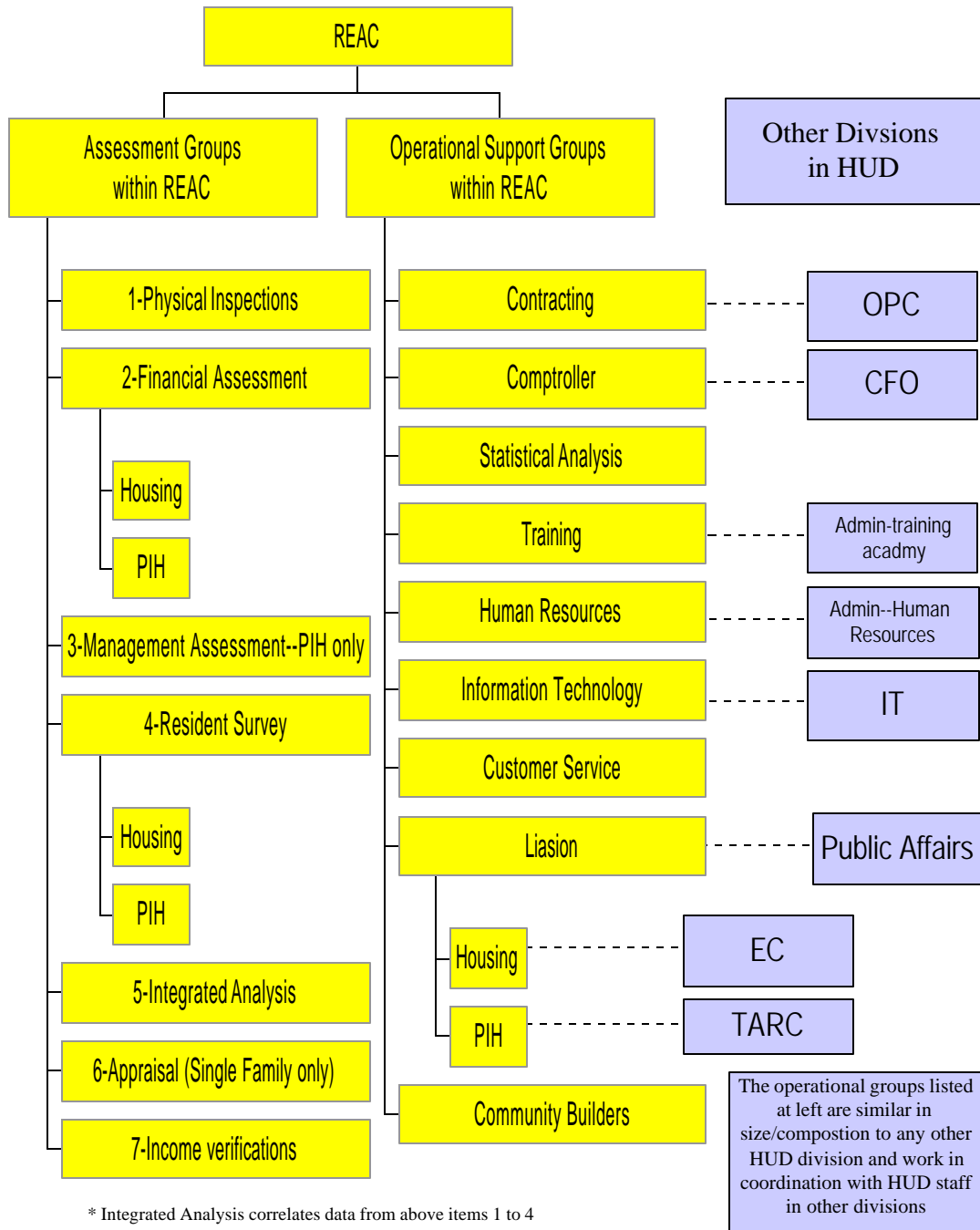
As stated previously, REAC is to assess the condition of the public housing authorities and the multifamily properties in which HUD has a financial interest. In this capacity, REAC has a dual mission: (1) to protect the public interest by identifying and assessing the risk of loss from physical deterioration of properties, financial insolvency and potential fraud waste and abuse and (2) to assist HUD in focusing its resources most effectively to raise the quality of the HUD housing portfolio, enhancing the quality of life for residents by helping to ensure decent, safe and sanitary housing.

HUD has been criticized for inadequate monitoring and enforcement of program regulations and requirements. In 1994, GAO designated HUD a "high risk". HUD developed plans for reinvention. The latest version, called HUD 2020 Management Reform, focused on organizational changes that did not require legislation. These organizational changes are intended to bring about operating efficiencies. The Real Estate Assessment Center has been called the cornerstone of the HUD 2020 plan.

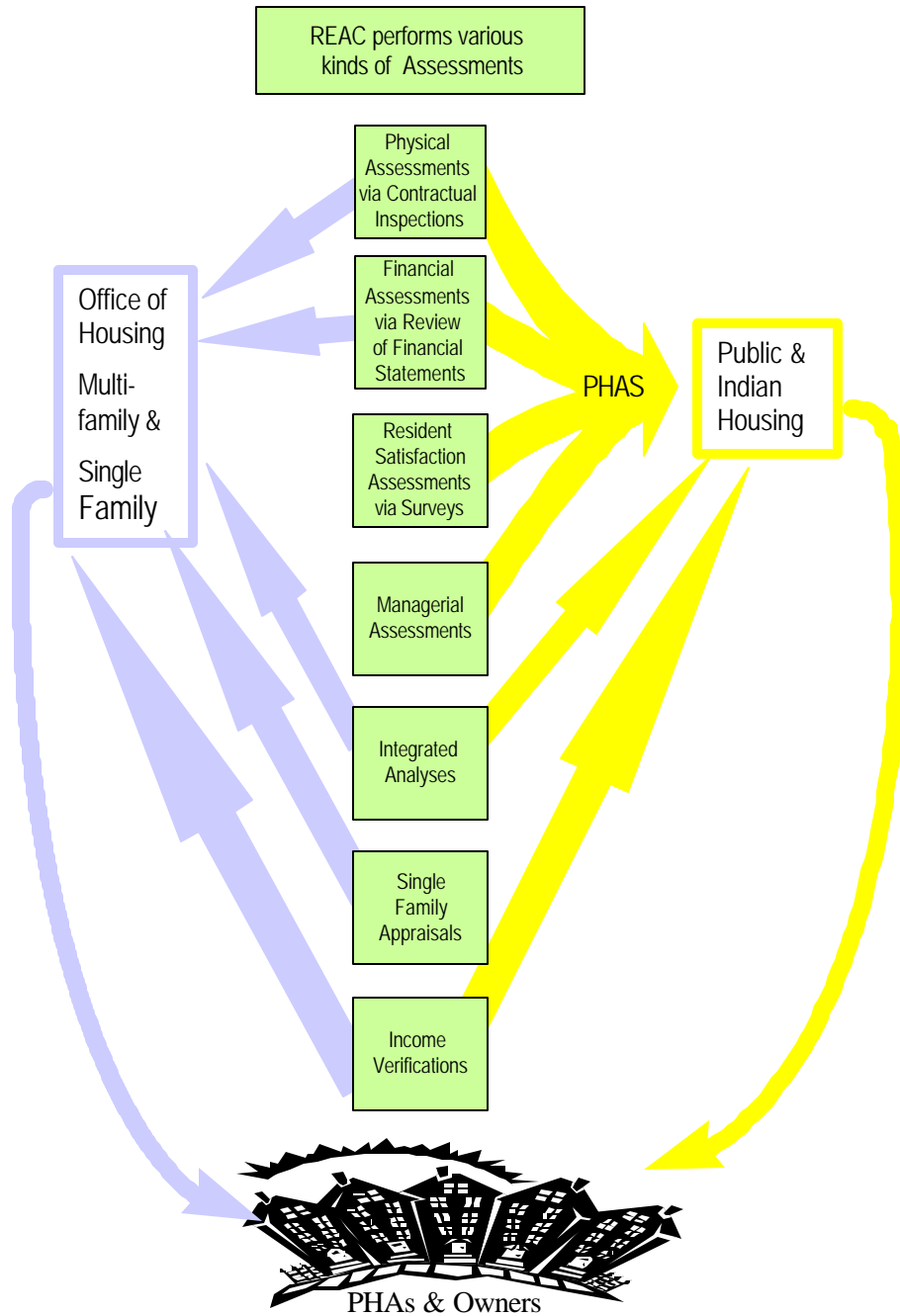
REAC's dual mission impacts on the Office of Public and Indian Housing and the Office of Housing (both multifamily housing and single family housing). At the same time, REAC is independent of these Offices. The Director of REAC reports to the Deputy Secretary as opposed to either the Assistant Secretary for Public and Indian Housing or the Assistant Secretary for Housing.

To accomplish its mission REAC has a staff ceiling of 213 full time personnel--many personnel are still being hired. As of March 31, 1999, 110 personnel were on board. REAC also resources other HUD Divisions as needed and has contracted with numerous external specialists, including Advanced Technology Systems, Andersen Consulting, Arthur Anderson, Arthur D. Little, KPMG Peat Marwick, Parsons Brinkerhoff Engineering, and PriceWaterhouseCoopers.

Based on REAC's staffing organization and interviews with REAC personnel, REAC has seven distinct types of assessments to perform. These assessments are supported by a number of operational groups. These operational groups relate to other divisions within HUD. Only physical inspections and financial assessments were in production at April 2, 1999. By production, we mean that the system is in use to perform its assigned function and should obtain valid results. The remaining assessments and their systems are still being developed by REAC.



As each assessment comes online, REAC provides the results of its assessments to the Office of Public and Indian Housing or the Office of Housing, as appropriate. Additionally copies of the assessments were being released to the public housing authorities and the multifamily owners.



The Inspection Process

REAC's inspection process includes:

- developing criteria to identify potential deficiencies in each inspectable item and assigning numeric values to deficiencies
- hiring and certifying contractors to perform inspections within a specific geographic locale
- performing inspections
- using the assigned numeric values to score inspections
- maintaining the consistency of the inspection process
- developing a process for appeals of scores.

REAC developed a system of over 800 inspectable items and assigned numeric values to potential deficiencies for each item. Two contractors were hired effective August 18, 1998 to evaluate the entirety of the public housing authority portfolio and one-third of the multifamily portfolio. On May 17, 1999, REAC hired additional contractors to perform inspections at the remaining properties within its assisted and subsidized portfolios. REAC has entered into six contracts under these two procurements and could spend up to \$117.4 million for inspections under these contracts.

For each inspection, a score is generated consisting of a numeric value between 1 and 100, a grade of a, b, or c identifying whether or not health and safety issues exist and an asterisk to identify if all smoke detectors are working. REAC has developed a two tier quality assurance program. The first tier is a Physical Assessment Standards Team who: perform desk reviews of inspections, adjust the training of contractors, and update the dictionary of observed deficiencies. The second tier is the Quality Assurance Inspection Team who evaluate the performance of contractual inspectors by re-inspecting properties.

OBJECTIVES AND SCOPE

The objective of our review is to assess the implementation of the Real Estate Assessment Center's operations pertaining to the physical inspections. This is one of seven types of assessments that REAC is performing.

We conducted our review from December 1998 to May 1999. To evaluate the efficiency and effectiveness of the implementation of REAC's contractual inspection service, we focused on

understanding REAC's operations, goals, and the systems that it was developing. We met with REAC's Acting Director, Deputy Director and members of their staff. We evaluated the contracts and task orders for the first procurement entitled the National Inspection Contracts and examined the second procurement entitled the Baseline Inspection Contracts in comparison to the first procurement. We accompanied a contractual inspection to experience the inspection process. We analyzed statistics for the results of over 11,000 inspections. We also evaluated REAC's quality assurance process.

**FINDING: REAC Has Not Yet Reached Full Implementation
Of Its Physical Inspection Assessment**

As the cornerstone of the HUD 2020 management reform plan, REAC is vital to successful implementation of the reforms needed to get HUD back on track. REAC has begun work on all seven of its assessments. We examined only the implementation of the physical inspection assessment. We have three concerns about the physical inspection assessment subsystem. Specifically we are concerned that:

1. On site quality assurance reviews only began after 11,000 inspections were completed;
2. A means of tracking findings and issues developed from the inspections has not been implemented; and
3. HUD has not determined that the benefits derived from the physical inspection assessment subsystem are commensurate with the cost of the subsystem.

While we are aware that full implementation is not yet complete, these concerns should be addressed for the physical inspection assessment subsystem to achieve success.

<p>Eleven thousand inspections were performed before on-site Quality Assurance Reviews began</p>

To ensure that inspections are performed in accordance with its contracts, REAC maintains two groups of professional inspectors—the Physical Assessment Standards Team and the Quality Assurance Inspection Team.

The role of the Physical Assessment Standards Team is to ensure data consistency and accuracy and to update the definitions used by the contractors. The Physical Assessment Standards Team performs desk reviews of the contractual inspections, adjusts the training of contractors, updates the dictionary of observed deficiencies and oversees the Quality Assurance Inspection Team (QA). REAC advises that standardization is the key to the physical inspection process.

The role of the Quality Assurance Inspection Team is to evaluate the performance of contractual inspectors. Through these evaluations, the Quality Assurance Inspection Team assure that contractual inspectors are uniformly interpreting the definitions in the physical inspection

software. The Quality Assurance Inspection Team also provides feedback on the software and recommends changes to the software.

The Quality Assurance Inspection Team became operational in May 1999. Inspections of subsidized properties by contractual inspectors began in October 1998. In the intervening seven months, over 11,000 inspections were performed by the contractors. Without onsite verification of the inspection process, HUD has very limited assurance that the contractual inspectors performed adequately for these 11,000 property inspections.

HUD needs its physical inspection assessments to be reliable in light of the reluctance of the assisted housing industry to embrace the new inspection subsystem. The various industry groups have expressed their reluctance through commentary on public notice, publicizing articles critical of the new assessment subsystems and suing HUD for failure to comply with federal requirements. HUD has responded to the industry by holding briefings at industry conferences, publishing additional Federal Registers notices to explain the physical inspection assessments and negotiating with the litigants for the withdrawal of the lawsuit.

AUDITEE'S RESPONSE AND ISSUE RESOLUTION

REAC states that its quality assurance program contains eight elements which were working to assist in assuring that the physical inspections were performed in accordance with the contract requirements. As a result of these elements, inspectors were either dismissed or suspended. REAC also states the conducting on site quality assurance review of properties inspected a year ago would serve no useful purpose since the deficiencies would not likely still be present. Based on REAC's response, the issue is considered resolved.

HUD does not have a method of tracking issues and findings developed from inspection results

HUD does not have a method to track issues and findings developed from contract inspection results. Without a system to identify how these issues and findings are addressed, HUD lacks assurance that identified problems at properties will be addressed. REAC staff have indicated that responsibility for overseeing the individual public housing authorities and multifamily properties continues to belong to the Office of Public and Indian Housing and the Office of Housing, respectively. REAC only performs assessments and does not resolve any project issues arising from those assessments.

Using data as of May 3, 1999, we examined the results of inspections on a national basis. Inspections have been performed in every state as well as every HUD district. Numerically, the scores are distributed

Numeric Scores between:	Number of Inspections	Percentage
0-30	400	3.4%
31-60	2053	17.7%
61-100	9147	78.9%
Total	11,600	100.0%

In each HUD district the majority of inspections received a numeric score that was greater than 60. Exigent health & safety issues were identified for 54.7% of the inspected properties.

Exigent Health & Safety issues:	Number of Inspections	Percentage
none	5257	45.3%
at least one non-life-threatening	3556	30.7%
at least one life-threatening	2787	24.0%
Total	11,600	100.0%

While the results of inspections show the properties to collectively be in fairly good condition, there is no assurance that individual properties with health and safety concerns or deficiencies in their physical condition will have these concerns corrected. Appendix A delineates the numerical and health and safety scores by district. For the 21.1% of the properties whose scores are below the standard and the 54.7% of the properties with health and safety concerns, correction of the deficiencies and concerns is needed.

The Acting Director of REAC and the Assistant Secretary of Public and Indian Housing have signed an agreement delineating the general operating relationships between their offices. In this agreement, REAC will 1) make electronic referrals to the appropriate PIH Office and 2) rely on the referred PIH office to seek information or corrective action.

There is no comparable signed agreement between REAC and the Office of Housing. The draft unsigned agreement between REAC and the Office of Housing states:

While assessment and enforcement actions have been delegated to the REAC and the Enforcement Center respectively, ultimate responsibility for the multifamily loan portfolio remains with Multifamily Housing.

Neither of these agreements contains any specifics about the tracking and resolution of issues developed from the inspection results. While responsibility for corrective action is delegated to staff other than REAC and the majority of inspections do not show serious problems, it remains vital to HUD that corrective action occurs. REAC only performs assessments and does not resolve any project issues arising from those assessments.

Discussions with officials from the Office of Housing indicate that they are requesting owners to certify the correction of any issues identified via the physical inspections. Housing advised that they are not verifying corrections at the project level because the Secretary assured the industry that only one inspection would be conducted each year. Discussions with officials from the Office of Public Housing indicate that they are developing a system to track corrective action for issues identified via the physical inspections.

To ensure that corrective action takes place, HUD needs to establish a means for tracking the resolution of issues developed from physical inspections performed by REAC or REAC's contractors. To be efficient, an assessment system must be utilized.

AUDITEE'S RESPONSE

REAC states that it is working with the Offices of Public and Indian Housing and the Office of Housing on risk management tools that include the issue of tracking identified deficiencies. In order for REAC to develop such a tracking system, REAC advised that it would have to reach agreement with both offices on the basic roles and responsibilities of each office. REAC would then develop the system requirements. REAC plans to initiate work on the feasibility of REAC being the catalyst for this project and plans to complete the protocol with the Office of Housing.

ANALYSIS OF AUDITEE'S RESPONSE

REAC concurs on the need for a tracking system, but does not state that it should take that role. If REAC determines that it is not feasible for REAC to fulfill this role, then HUD needs to determine which division should fulfill that role. Completion of the protocol between the Office of Housing and REAC would be instrumental in determining which division of HUD should fulfill that role. REAC and the Office of Public Housing have signed a protocol detailing their responsibilities. This protocol does not mention the tracking of issues developed from REAC's assessments.

HUD has not determined that the benefits are commensurate with the cost of the physical inspection assessment subsystem.

In developing its systems, REAC has focused on the benefits to be derived from the systems without specifically considering the cost of developing, operating and maintaining the systems in comparison with the cost of existing operations.

HUD has budgeted over \$62.9 million from the *salaries and expenses* appropriation and the *working capital fund* to develop all of the assessments and maintain REAC.

FY	Assessment Subsystems	Salaries and Operations
1998	\$14.8 million	\$2.4 million
1999	\$34.7 million	\$11.0 million

For its physical inspection assessment subsystem, REAC has entered into six contracts under two different procurements. The first procurement is called the National Inspection Contracts (NIC). The three contracts under NIC have an initial term of one year with four one year renewal options. Under the terms of the three NIC contracts, HUD could pay out up to \$57.4 million for 90,000 inspections. The second procurement is called the Baseline Inspection Contract (BIC). The three contracts under BIC are indefinite quantity contracts. Under the terms of the three BIC contracts, HUD could pay out up to \$60 million for inspections. Inspections are paid out of the appropriations supporting the creation of the projects and not out of *salaries and expenses* appropriation or the *working capital fund*.

Prior to the creation of the physical inspection assessment subsystem, the function of performing physical inspections was one of many duties assigned to field staff within the Office of Public Housing or the Office of Housing, as appropriate. In prior reviews, OIG has advised that adequate monitoring, including physical inspections, was not being performed. Having annual inspections of subsidized properties benefits HUD by providing that monitoring. However, we remain concerned about whether the benefits derived from REAC's physical inspection assessment subsystem outweigh the cost of the subsystem. HUD should perform a cost-benefit analysis of REAC physical inspection assessment subsystem.

With the establishment of an inspection baseline through the NIC and BIC procurements, HUD needs to determine if annual re-inspection of 100% of the subsidized properties is cost-effective. With the standardization of criteria and the objective measures provided through the physical inspection assessment subsystem, HUD has consistent and objective measures for each property inspected.

Cost:Resources:Benefits



HUD has the opportunity to use this baseline to evaluate the benefits of the inspection assessment system against its available resources and its managerial needs. To take full advantage of this opportunity and make a thoughtful decision regarding the best way to operate, HUD needs to evaluate the cost of the inspection assessment system in light of the resources available to HUD as well as in light of the benefits derived from the standardization of inspections.

AUDITEE'S RESPONSE

REAC concurs with the need for a cost benefit analysis and has performed several analyses of proposed operations including a Cost Benefit analysis dated July 16, 1998.

ANALYSIS OF AUDITEE'S RESPONSE

Our examination of the Cost Benefit Analysis dated July 16, 1998 identified that it extrapolated the costs of operating REAC by specifically identifying the recurring and non-recurring costs. The Cost Benefit Analysis also identified the benefits to be derived from creating REAC in comparison with the flaws of the existing system.

As its scope, the Cost Benefit Analysis lists:

This Cost/Benefit Analysis will analyze the REAC and its underlying automated systems. The analysis is meant to be a general overview of the costs associated with the development implementation an operation of the REAC

The Cost Benefit Analysis does not compare operating costs of the preceding operations to REAC's operations. Regarding cost estimates, the Cost Benefit Analysis states:

The REAC represents a fundamental shift in the way HUD conducts its business. It utilizes ground breaking technology and creates business processes unlike anything existing in the

inspection and assessment industries today. Therefore, the costs cannot be extrapolated from projects of a similar nature nor can an exact methodology be used for estimation. This does not mean, however that the costs contained in the cost worksheet are without merit. The REAC development team has drawn upon its years of experience and extensive knowledge of HUD program to create a budget and supplement worksheets from which the cost figures were derived.

The Cost Benefit Analysis also does not compare the benefits derived from preceding operation to REAC's operations. Regarding benefits, the Cost Benefit Analysis states:

The benefits of a centralized real estate assessment center that utilizes a standardized automated assessment system may not be easily measure in dollars and cents. They are however critical to the re-invention of HUD and represent a profound improvement in the assessment of HUD's portfolio of properties.

Even if the benefits are qualitative rather than quantitative, the benefits derived from REAC should be measurable and should be compared to the benefits derived preceding operations.

RECOMMENDATIONS

We recommend that HUD:

- 1A. Establish a means for tracking the resolution of issues developed from physical inspections performed by REAC or REAC's contractors.
- 1B. Complete and execute the agreement between the Office of Housing and the Real Estate Assessment Center that delineates the general operating relationships between these two offices.
- 1C. Perform a cost-benefit analysis of REAC's physical inspection assessment showing how HUD has evaluate the cost of the inspection assessment system in light of the resources available to HUD as well as the benefits derived from the standardization of inspections.

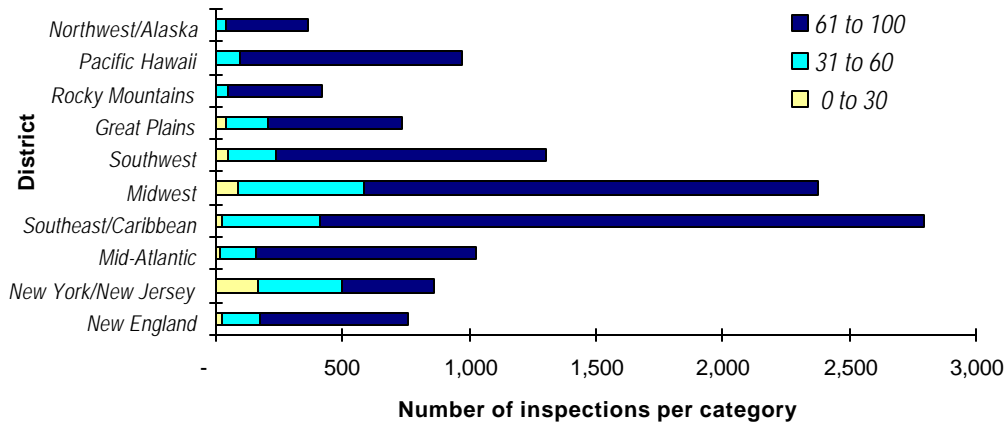
Appendix A

NATIONAL STATISTICS ON INSPECTIONS

as of May 3, 1999

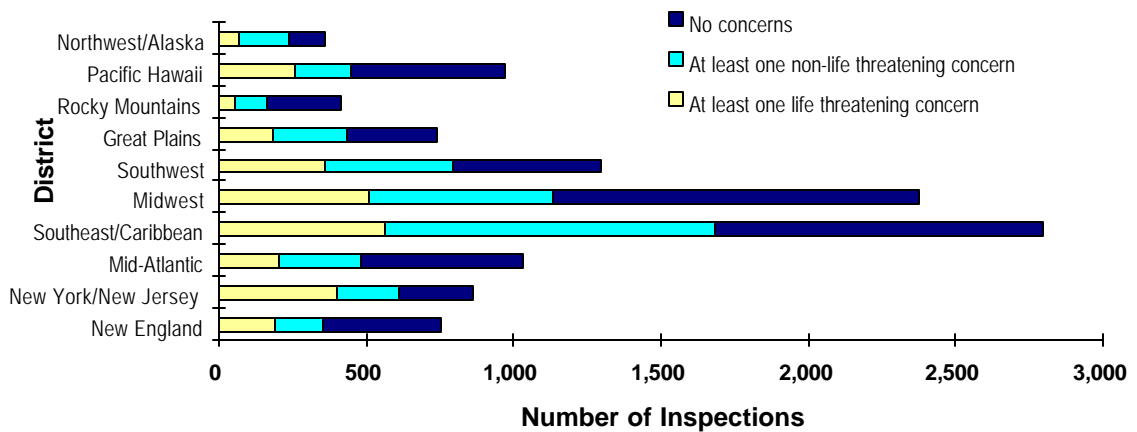
Inspections have been performed in every state as well as every HUD district as follows:

Inspection Scores



The majority of inspections received a numeric score that was greater than 60. Exigent health & safety issues exist and need to be corrected.

Exigent Health & Safety Concerns



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U. S. Department of Housing and Urban Development
1280 Maryland Avenue, SW
Suite 800
Washington, D.C. 20024-2135

REAL ESTATE ASSESSMENT CENTER

SEP 21 1999

MEMORANDUM FOR: William D. Hartnett, District Inspector General, Office of
Audit, IAGA

FROM:  Donald J. LaVoy, Acting Director, Real Estate Assessment Center

SUBJECT: Implementation of the Real Estate Assessment Center's Physical Inspection
Assessments

This is in reply to your memorandum of August 30, 1999, providing
recommendations after concluding the subject review.

Our response to your specific findings and recommendations are as follows:

1. Recommendation - 1A. Confirm the accuracy of the inspection results for the 11,000 properties inspected to show that the Department of Housing and Urban Development (HUD) has reliable results for all of its inspections.

The Real Estate Assessment Center (REAC) Response. REAC's quality assurance program for physical inspections is not limited solely to on-site reviews. Instead, the REAC quality assurance involves eight other elements on different levels, all working to assist in assuring that the physical inspections raised in this recommendation were performed in accordance with contract requirements. These elements were all at work during the time period in question.

The REAC quality assurance program includes the following:

- A. The Physical Inspection Operations Division is responsible for reviewing inspections that are uploaded to the REAC from contract inspectors. This Division developed operating procedures and performed reviews on 100% of the inspections that were received electronically from the inspectors, including inspections performed between October 1998 and May 1999. Any problems identified as a result of this review were brought to the attention of the respective contractors for corrective action and resolution. In addition, REAC had monthly

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meetings with the contractors to convey concerns regarding the quality of the inspections.

- B. The Statistical Analysis Division analyzed 100 % of the physical inspections, scores, and inspectors to determine the presence of outliers. REAC provided feed back to its contractors regarding the performance of the inspectors.
- C. The Standards Division conducted independent analysis and/or reviews of inspections between October 1998 and May 1999 as follows:
 - Performed desk reviews on scores less than 60 points to ensure that deficiencies noted matched definitions;
 - Conducted Limited Quality Assurance (LQA) inspections of properties within 100 miles of the District of Columbia;
 - Performed collaborative inspections that identified inspectors that were not following the REAC protocol. As a result of these collaborative inspections, inspectors were either dismissed or suspended.
- D. Quality Assurance Division. The Quality Assurance Division did perform on-site reviews of a statistically valid sample (approximately 183) of the inspections between November 4 and April 16.
- E. Customer Service Center (CSC). REAC established a CSC with a toll free telephone number and an e-mail address. The CSC is available to all program participants and has been open since the inception of the inspection program. The CSC is a focal point for program participants who have problems or question to get those issues resolved. It also provides the REAC with intelligence regarding the quality of REAC work, including physical inspections. Problems that were identified during this period from the CSC were subsequently referred to the Government Technical Representative for resolution.
- F. Technical Reviews. HUD published a notice in the Federal Register on May 13, 1999, to permit public housing agencies to request a technical review of their inspections in cases of certain contractor errors. A similar provision is being developed for the Multifamily Housing Programs. The technical reviews provide the REAC with data regarding the quality of the first inspections performed during the period in question.
- G. Outreach. The REAC has done extensive outreach by meeting with industry groups around the country. During these sessions, owners/PHAs are encouraged to provide REAC with information on potential inspector mistakes. Where feed back was provided, REAC followed up on those issues raised.
- H. Training. REAC requires each inspector to attend an 80-hour training course and pass a certification test demonstrating proficiency in the use of the inspection

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software, including deficiency classification. In addition, based on feed back noted in the above elements that reflects contractor performance during the time period in question, REAC provided additional remedial training to inspectors on several occasions to ensure acceptable performance.

Based on the above actions, the REAC quality assurance program was in operation during the time period in question. There were sufficient on-going activities to provide reasonable assurances that the inspections performed before May 1999 met contract requirements. In addition, it has become evident from our discussions with owners, the industry and program offices that the past culture of neglect is changing. Owners now know that the Federal government will be making on-site inspections of their property and are taking actions to correct deficiencies before and after the REAC inspections. Given this fact, even if REAC had not done all of the activities described above, conducting on-site quality assurance reviews of properties inspected a year ago would serve no useful purpose since the deficiencies would not likely still be present. Moreover, REAC inspections are still an annual event. New inspections are being scheduled and will yield new information about the condition of the properties. REAC, therefore, concludes that no further action is necessary on this recommendation.

2. Recommendation – 1B. Establish a means for tracking the resolution of issues developed from the physical inspections performed by REAC or REAC’s contractors.

REAC Response. As previously noted, REAC is a data collection and dissemination agency. The Offices of Public and Indian Housing, and Housing as well as the REAC have responsibility for establishing operating procedures to respond to the results of the physical inspections performed by the REAC. Offices Public and Indian Housing and Housing have issued operational instructions to their respective field offices. The REAC is working with these Offices on risk management tools that include the issue of tracking REAC identified deficiencies. In order for the REAC to develop such a tracking system, REAC would have to reach agreement with both offices on the basic roles and responsibilities of each office. REAC would then develop the system requirements. We will initiate work on the feasibility of REAC being the catalyst for this project and report back to your office by December 31, 1999.

3. Recommendation - 1C. Complete and endorse the agreement between the Office of Housing and the Real Estate Assessment Center that delineates the general operating relationships.

REAC Response. REAC will complete the protocol effort that will include guidebooks, training and the agreement with the Office of Housing. We have targeted December 31, 1999 as the date by which this will be accomplished.

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4. Recommendation – 1D. Perform a cost benefit analysis of REAC's physical inspection assessment.

REAC Response. REAC agrees with your Office in the need for analyzing the costs and benefits of new programs. In developing the REAC itself and in particular the physical inspection system, REAC did a number of studies and research, including a cost benefit analysis, to determine if the REAC and the physical inspection system were justified. The REAC was assisted in these efforts by KPMG-Peat Marwick. As you are aware, HUD has approximately 40,000 properties in its portfolio of multifamily insured, Section 8 project based, public housing and other properties. The capital outlay, initial and on-going, for these programs is in the billions of dollars. REAC found that the nominal costs of the assessment system were clearly justified based on the numerous benefits, tangible and intangible, that the Federal government derived from REAC inspections. One of the most significant benefits derived is the restoration of the public trust in HUD's mission to provide decent, safe, sanitary housing that is in good repair.

These studies included in the following:

- A. August 4, 1997, KPMG-Peat Marwick research and evaluation of computer inspection systems.
- B. August 11, 1997, KPMG-Peat Marwick summarization and analysis of computerized inspection system.
- C. October 27, 1997, KPMG-Peat Marwick options and evaluation for hand held data collection devices.
- D. November 13, 1997, KPMG-Peat Marwick response to comments on evaluation for hand held data collection devices.
- E. December 1, 1997, KPMG-Peat Marwick summary of test results using four different DCDs.
- F. July 16, 1998, REAC Cost Benefit Analysis.
- G. July 1998, REAC Front End Risk Assessment.

Based on the above, a cost benefit analysis was completed and no further action is necessary regarding this recommendation.

The REAC would also like to comment on your Office's suggestion that we should reconsider the inspection of each project on an annual basis. The Assistant Secretary for Public and Indian Housing stated that projects that consistently score high do not need annual inspections. In this regard, we call your attention to the proposed revisions to the Public Housing Assessment System (PHAS) regulations published on June 22, 1999. You will note that the Subpart G of the rule proposes that physical inspections for "high performers" be performed once every other year for any project that receives an inspection score of 90 or higher. There are similar regulatory amendments being drafted

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for the multifamily programs that are currently in development. As we progress and expand the database, REAC will re-examine this issue further and make adjustments as seem prudent.

I hope that the above adequately responds to the recommendations made in your review. Copies of documentation supporting our responses are available upon request. If you have any further questions and/or need any assistance please feel free to contact Bill Thorson at (202) 708-4932 extension 3005.

cc:

Saul Ramirez
Harold Lucas
William Apgar

Appendix C

Distribution

Deputy Secretary, SD, Room 10100 (1)
Chief of Staff, S, Room 10000 (1)
Special Assistant to the Deputy Secretary for Project Management, SD, Room 10100 (1)
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Assistant Secretary for Congressional and Intergovernmental Relations, J, Room 10120 (1)
Senior Advisor to the Secretary, Office of Public Affairs, S, Room 10132 (1)
Director of Scheduling and Advance, AL: Room 10158 (1)
Counselor to the Secretary, S, Room 10234 (1)
Deputy Chief of Staff, S, Room 10226 (1)
Deputy Chief of Staff for Operations, S, Room 10226 (1)
Deputy Chief of Staff for Programs and Policy, S, Room 10226 (1)
Deputy Assistant Secretary for Public Affairs, W, Room, 10222 (1)
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Executive Officer for Administrative Operations and Management, S, Room 10220 (1)
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Director, Office of Federal Housing Enterprise Oversight, O, 9th Floor Mailroom (1)
Assistant Secretary for Housing Federal Housing Commissioner, H, Room 9100 (1)
Office of Policy Development and Research, R, Room 8100 (1)
Inspector General, G, Room 8256 (1)
Assistant Secretary for Community Planning and Development, D, Room 7100 (1)
Government National Mortgage Association, T, Room 6100 (1)
Assistant Secretary for Fair Housing and Equal Opportunity, E, Room 5100 (1)
Chief Procurement Officer, N, Room 5184 (1)
Assistant Secretary for Public and Indian Housing, P, Room 4100 (1)
Chief Information Officer, Q, Room 3152 (1)
Director, Office of Department I Equal Employment Opportunity, U, Room 5128 (1)
Director, Office of Departmental Operations and Coordination, I, Room 2124 (1)
Chief Financial Officer, F, Room 2202 (1)
Director, Enforcement Center, V, 200 Portals Building (1)
Director, Office of Multifamily Assistant Restructuring, Y, 4000 Portals Building (1)
Secretary's Representative (20—2 each)
Assistant Deputy Secretary for Field Policy and Management, SDF, Room 7108 (2)
Deputy Chief Financial Officer for Finance, FF, Room 2202 (1)
Director, Office of Budget, FO, Room 3270 (1)
Primary Field Audit Liaison Officer, 3AFI, (2)
Headquarters Audit Liaison Officer, SD, Room 10126, (2)
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Acquisitions Librarian, Library, AS, Room 8141 (1)
Deputy Inspector General, G, Room 8256 (1)
Assistant Inspector General for Audit, GA, Room 8286 (1)
Deputy Assistant Inspector General for Audit, GA, Room 8286 (1)
Assistant Inspector General for Investigation, GI, Room 8274 (1)
Special Agent-In-Charge, 1AGI, (1)
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Director, Financial Audits Division, GAF, Room 8286 (1)
Director, Information Systems Audit Division, GAA, Room 8172 (1)
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