
AUDIT REPORT



GOLDEN FEATHER REALTY SERVICES, INC.
MANAGEMENT AND MARKETING CONTRACTOR FOR
ATLANTA AREA A-1

CHICAGO, ILLINOIS

00-CH-211-1005

SEPTEMBER 26, 2000

OFFICE OF AUDIT, MIDWEST
CHICAGO, ILLINOIS



Issue Date	September 26, 2000
Audit Case Number	00-CH-211-1005

TO: Charles E. Gardner, Director, Atlanta Homeownership Center

FROM: Dale L. Chouteau, District Inspector General for Audit, Midwest

SUBJECT: Golden Feather Realty Services, Inc.
Management and Marketing Contractor
Chicago, Illinois

We completed an audit of Atlanta Homeownership Center's Management and Marketing contractor, Golden Feather Realty Services, Inc., for Atlanta Area A-1. The audit was conducted as part of a nationwide internal audit of the Federal Housing Administration's Single Family Property Disposition Program. The objectives were to determine whether Golden Feather managed HUD's single-family disposition program in accordance with HUD policies, procedures, and regulations and with the terms and conditions of Golden Feather's Management & Marketing Contract.

The audit disclosed that Golden Feather did not provide sufficient oversight of appraiser work assignments necessary to discourage the solicitation of a kickback. In addition, Golden Feather did not execute or record land use restriction addendums necessary to restrict nonprofit organizations from purchasing properties at a 30 percent discount and reselling the properties for more than 110 percent of the cost. Furthermore, Golden Feather did not always maintain properties, use approved appraisers to appraise HUD properties, and process appraisals and disposition programs timely.

Within 60 days, please provide us, for each recommendation made 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 provide us copies of any correspondence or directives issued because of the audit.

Should you or your staff have any questions, please contact me at (312) 353-7832.

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Executive Summary

We completed an audit of Golden Feather Realty Services, Incorporated (Golden Feather). The primary purpose of our audit was to determine whether Golden Feather managed HUD single-family properties in accordance with HUD policies, procedures, and regulations and with the terms and conditions of its management and marketing contract. This included determining whether Golden Feather's operations were effective, efficient and economical and management controls effectively identified and addressed operational deficiencies.

On September 22, 1999, Golden Feather began to manage and market HUD properties located in the states of Illinois, Kentucky, Tennessee and Indiana. Golden Feather demonstrated success in two key areas. First, the contractor reduced the number of properties in inventory and second the contractor increased the number of insured and uninsured property sales to owner occupants, investors, nonprofit organizations and government agencies. Golden Feather's inventory reduction efforts in the state of Illinois were acknowledged nationally with the awarding of HUD's "Best Practices" Award in the Summer of 2000. Despite these accomplishments, improvements were still needed.

Golden Feather's management controls were weak over assigning appraiser work assignments, restricting re-sales for nonprofit organizations, maintaining properties, using approved appraisers and processing inventory timely.

Oversight of Appraiser Work Assignments Needs Strengthening

Golden Feather's management controls did not provide reasonable assurance that employees did not exceed or abuse their assigned authorities. Due, in part, to the lack of separation of duties and supervisory oversight, a Golden Feather employee was able to solicit a kickback from two appraisers in exchange for increased work assignments. In addition, Golden Feather did not notify the OIG of the solicitation as prescribed by the Federal Acquisition Regulations.

Controls over Resale Restrictions for Nonprofit Organizations were Weak

Management controls necessary to help deter nonprofit organizations from abusing HUD's discount sales program were weak. Land use restrictions were not executed or recorded for properties sold to nonprofit organizations at a 30 percent discount. The restrictions prohibit nonprofit organizations from purchasing properties at a 30 percent discount and reselling them for more than 110 percent of cost. The restrictions also prohibit sales to parties that did not intend to occupy the property as a principal residence. Because the land use restrictions were not executed or recorded, several nonprofit organizations resold properties to trusts and investors that resold the properties for amounts ranging between 177 percent and 597 percent greater than

the HUD discounted sales amount. Some properties were resold on the same day the nonprofit organization purchased the property from HUD and multiple properties were sold to the same buyer.

Properties Not Maintained

Weak management controls over property inspections and correcting reported deficiencies resulted in poor inspections and deficiencies not being corrected. A review of 26 properties disclosed that Golden Feather did not always: (1) identify serious health and safety deficiencies; (2) correct reported hazardous conditions within mandatory 24 hours; (3) properly secure properties; (4) ensure that properties were protected from the elements; (5) identify defective paint; and (6) maintain each property in a presentable condition at all times. Additionally, Golden Feather did not always take corrective action on reported deficiencies. Poor property conditions contribute to performance problems such as decreased marketability, increased costs, possible decreased value of surrounding homes, and possible conditions that threaten the health and safety of neighbors and potential buyers.

Unapproved Appraisers used for HUD Properties

Golden Feather did not ensure appraisers were HUD approved appraisers. Four appraisal companies appraised 213 properties using seven unapproved appraisers. Officials believed HUD-approved supervisory appraisers could supervise unapproved appraisers. However, supervisory appraisers were not always present during the physical appraisal. Because unapproved appraisers were used, HUD's risk in obtaining an inaccurate list and sales price has been increased.

Untimely Appraisals and Disposition Programs

Golden Feather's management controls did not always prevent untimely appraisals and disposition programs. Four of 29 properties were appraised from six to 56 days late. Nine of 29 property disposition programs were approved from one to 50 days late.

Delays in obtaining property appraisals and approving disposition programs cause properties to remain in HUD's inventory longer than necessary, resulting in additional property holding costs and exposure to vandalism.

Recommendations

We recommend that you ensure Golden Feather: (1) establish and implement procedures to provide supervision, segregate key duties of its employees within the New

Acquisitions Departments and comply with Anti-Kickback Act reporting requirements; (2) execute and record land use restrictions for sales to nonprofit organizations; (3) develop and implement oversight procedures for inspections; and (4) report and correct the hazards and other maintenance deficiencies identified by OIG and Golden Feather's inspectors. We further recommend that you ensure Golden Feather uses HUD-approved appraisers, require the contractor to obtain new appraisals for the insured properties that were appraised by unapproved appraisers, and ensure the contractor develops and implements controls for processing appraisals and disposition programs timely.

We discussed the findings in this report with Golden Feather's staff during the course of the audit. On August 11, 2000 and on August 23, 2000 we provided Golden Feather a copy of the draft audit findings for comment. We received Golden Feather's written responses on August 21, 2000 and on August 26, 2000. In general, Golden Feather disagreed with the contents of the report. Appropriate revisions were made where deemed necessary. We included Golden Feather's pertinent comments in the findings section of this report. Golden Feather's full response is included in Appendix B.

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Introduction

HUD disposes of properties through its Property Disposition Program, administered by the Office of Single Family Housing Real Estate Owned Division. Its mission is to reduce the property inventory in a manner that expands homeownership opportunities, strengthens neighborhoods and communities, and ensures a maximum return to the mortgage insurance fund. The National Housing Act of 1934 confers on the Secretary the authority to manage, rehabilitate, rent and dispose of its acquired single-family properties. Section 204(g) of the Act governs the management and disposition of acquired single-family properties. Title 24, Code of Federal Regulations, part 291 implements the statutory authority. Handbook 4310.5 REV-2, Property Disposition Handbook - One to Four Family Properties, supplements the regulations.

In 1993, HUD initiated a reinvention effort to streamline operations and reduce costs. HUD began reducing program staff and consolidating its mortgage insurance processing, claims, and property disposition activities from the field into four Homeownership Centers. The centers are located in Santa Ana, California; Denver, Colorado; Atlanta, Georgia; and Philadelphia, Pennsylvania.

In March 1999, HUD contracted the management and marketing of properties that were owned by or in the custody of HUD. Seven contractors were awarded a total of 16 Management and Marketing contracts nationwide. The contractors assumed full responsibility for the management and marketing functions. In September 1999, HUD announced it terminated its contract with InTown Management Group. InTown Management Group was responsible for properties located in the Atlanta Area A-1. At the time the contract was terminated InTown Management Group had an inventory of approximately 5,600 properties.

Golden Feather was awarded the replacement contract for the Atlanta Homeownership Center Area A-1 effective September 1999. Atlanta Area A-1 consists of properties located in Illinois, Indiana, Kentucky and Tennessee. The total duration of this 16-month contract shall not exceed five years, including the exercise of any options. The total estimated value of the contract is \$74 million. Golden Feather also manages and markets HUD's single-family properties for the Santa Ana Homeownership Center Areas C-1, C-2 and C-3.

During the audit period, Golden Feather was responsible for managing and marketing an average inventory of over 4,800 properties in Atlanta Area A-1. As of July 31, 2000, Golden Feather had 3,532 properties in its inventory for the four-state area.



Audit Objective

The audit objectives were to determine whether Golden Feather managed HUD single-family properties located in Atlanta Homeownership Center's Area A-1 in compliance with HUD policies, procedures and regulations and with the

Audit Scope and
Methodology

terms and conditions of the contract. This included determining whether Golden Feather's (1) operations were effective, efficient and economical, and (2) management controls effectively identified and addressed operational deficiencies.

The audit covered the period October 1, 1999 to July 31, 2000. We performed our on-site audit work between May and August 2000. We conducted the audit at Golden Feather's Chicago, Illinois office. The audit was conducted in accordance with generally accepted government auditing standards.

To determine whether Golden Feather managed HUD's single family properties in accordance with HUD policies, procedures, regulations and contract requirements, we:

- Reviewed HUD Handbooks, Office of Management and Budget Circulars, the Anti-Kickback Act of 1986, the Management and Marketing contract and Federal Regulations;
- Reviewed Performance Assessment reports and third-party contractors' monitoring reports;
- Reviewed Golden Feather's policies and procedures;
- Tested Golden Feather's internal controls by interviewing staff and reviewing transactions, testing procedures and observing operations;
- Reviewed twenty nine active cases, eighteen closed property case files and ten held off market cases, the cases reviewed were selected on a random judgmental basis;
- Performed 26 property inspections; 12 in Chicago, Illinois and 14 in Indianapolis, Indiana, the cases reviewed were selected on a random judgmental basis;
- Reviewed contractor payment vouchers and public property records;

- Conducted interviews with Golden Feather staff and management, subcontractors, and Atlanta Homeownership Center personnel.

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Oversight of Appraiser Work Assignments Needs Strengthening

Golden Feather did not maintain a separation of duties within the New Acquisitions Department and did not provide supervisory oversight of the Department's manager. The Department manager had sole responsibility for selecting and issuing work orders to appraisers. The manager's work was not monitored as closely as it should have been. The manager solicited kickbacks from two appraisers in exchange for awarding the appraisers work assignments. Golden Feather learned about the solicitations only after the two appraisers complained about the solicitation. After consulting with HUD's Atlanta Homeownership Center, Golden Feather dismissed the manager. Additionally, Golden Feather did not notify the OIG as required by its contract. We learned of the solicitation only after our auditors made inquiries about the manager's absence and from the Atlanta Homeownership Center.

Sound internal controls are an integral part of the process.

HUD Handbook 4310.5, Property Disposition Handbook - One to Four Family Properties, stresses the importance of internal control procedures as an integral part of Single Family Property Disposition processing. Control procedures are those policies and procedures that management has established to provide reasonable assurance programmatic and financial management objectives will be achieved. They pertain in part to segregation of duties that reduce the opportunity to allow any person to be in a position to both perpetrate and conceal errors or irregularities in the normal course of duties. This includes assignment to different staff of responsibility for authorizing Single Family Property disposition transactions, recording transactions, and maintaining custody of the properties.

OMB Circular A-123, Management Accountability and Control, identifies separation of duties and supervision as a specific management control standard. The standard states that key duties and responsibilities in authorizing, processing, recording, and reviewing official agency transactions should be separated among individuals. Managers should exercise appropriate oversight to

ensure individuals do not exceed or abuse their assigned authorities.

Duties were not segregated.

The duties within the New Acquisition Department were not segregated. The manager had sole responsibility for selecting appraisers and issuing work orders to appraisers beginning in March 2000. The apparent kickback solicitations occurred in May 2000. One employee assisted with the work assignments from November 1999 through March 2000. In March the manager told the employee he would assume all duties related to the assignment of work orders. A review of the Department's staffing levels disclosed the change in work assignment was not due to a staffing shortage. Two staff members occasionally issued work orders while the manager was on leave. This was infrequent and under the manager's control.

The manager of the Department was not properly supervised.

Golden Feather's contract manager said he did not believe the manager's work was monitored as closely as it should have been. He believed the lack of oversight occurred because the Department appeared to be running well. A review of Golden Feather's policy and quality manuals disclosed that monitoring requirements for the Department were not included in the manuals. A review of the Department's records disclosed the absence of any documents related to the oversight of the Department.

The day after our interview with the contract manager, the vice president of Golden Feather informed us that the contract manager was incorrect in his assessment. The vice president also said that this event was regrettable but it was not preventable.

Contrary to the vice president's opinion, we believe proper segregation of duties and oversight could have prevented the event.

Golden Feather did not notify OIG of the kickback solicitations.

Golden Feather did not notify OIG of the Manager's kickback solicitations as required by its contract and the Federal Acquisition Regulations.

Section 52.203-07 of the Federal Acquisition regulations states when the contractor has reasonable grounds to believe that a violation may have occurred, the contractor shall promptly report in writing the possible violation. Such reports shall be made to the OIG of the contracting agency, the head of the contracting agency if the agency does not have an OIG, or the Department of Justice. The OIG was not notified of the violation. The OIG discovered the violation through the normal course of the audit.

Auditee Comments

Excerpts from Golden Feather's comments follow. Appendix B contains the complete text of the comments.

Golden Feather's internal controls were comprehensive and sufficient to discover the wrongful act before a kickback was paid and before any influence was exerted. Because of the early detection and rapid response, neither HUD nor Golden Feather was victimized by this employee's conduct.

Golden Feather's controls assured that key duties in authorizing, reviewing and paying for contractors' work (including appraisers) were separated among different individuals and different offices. We disagree with the finding that the responsibilities of selecting appraisers and issuing work orders must be separated.

Contrary to the statements made in this report, the Office of the Inspector General was notified of this issue by the Director of the Atlanta Homeownership Center immediately upon discovery of the alleged conduct and the Office of Inspector General was aware of the matter four days prior to the employee's dismissal. The intent of Section 52.203-07 of the Federal Acquisition Regulations is to assure that the Office of Inspector General is made aware of potential violations. In this instance, the intent of this regulation was unquestionably fulfilled.

OIG Evaluation of
Auditee Comments

We disagree that Golden Feather's management controls were comprehensive and sufficient to discover the kickback solicitation. Golden Feather's management controls did not discourage, identify, or prevent the kickback solicitations. Golden Feather's own contract manager believed the employee was not properly supervised.

Golden Feather stated it relied on its relationship with its contractors to report unlawful acts as part of its management controls. Our interviews disclosed that the whistleblowers contacted HUD and the Golden Feather's home office in San Antonio, Texas due to the lack of confidence or familiarity they had with Golden Feather's staff in Chicago, Illinois. We also disagree that relying on sub-contractors to report illegal acts is part of a good management control structure.

Contrary to Golden Feather's response, appraisal documents did not indicate that key duties in authorizing and reviewing appraisal work orders were separated among different individuals. There were no indications of a segregated review.

Golden Feather's actions indicate they believed the oversight of appraisers work assignments did need strengthening. On August 1, 2000, Golden Feather implemented a comprehensive policy statement, action plan, and audit control specifically designed to detect and prevent potential business abuses by employees or contractors. However, we did not test the new policy and believe that it should not be relied on without testing.

We also disagree that Golden Feather complied with the Anti-Kickback reporting requirements. The Federal Acquisition regulations require that when a contractor has reasonable grounds to believe a violation may have occurred, the contractor shall promptly report in writing the possible violation. Such reports shall be made to the Office of Inspector General. Golden Feather did not report the violation in writing to the Office of Inspector General.

Recommendations

On June 23, 2000, we issued a memorandum to the Director of the Atlanta Homeownership Center recommending the initiation of debarment procedures against the former manager. The Director concurred with the recommendation and initiated the process for a limited denial of participation and plans on initiating the debarment process as soon as the limited denial of participation appeal process has expired.

We also recommend that the Director of the Atlanta Homeownership Center:

- 1A. Assures that Golden Feather segregates key duties and responsibilities in the New Acquisitions Department for authorizing appraisal work orders and selecting appraisers to perform the work orders.
- 1B. Assures that Golden Feather establishes and implements procedures for the oversight of the manager.
- 1C. Assures that Golden Feather establishes and implements procedures to comply with the Anti-Kickback Act's reporting requirement.

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Controls over Resale Restrictions for Nonprofit Organizations were Weak

Golden Feather did not execute or record land use restriction addendums. The addendum, which restricts nonprofit organizations from purchasing properties at a 30 percent discount and reselling them for more than 110 percent of the net development cost, is required with each sales contract. The addendum also requires organizations to resell properties to individuals who intend to occupy them as a principal residence. Golden Feather attributes the oversight to misinterpreting an Atlanta Homeownership Center instruction. Because the addendums were not executed or recorded, resale amounts may have exceeded the restriction amount and properties may not have been sold as a principal residence.

Contract restricts re-sale.

Exhibit two of the contract states that properties purchased by a nonprofit organization at a 30 percent discount are primarily intended to be resold to persons who are at or below 115 percent of median income for their area, when adjusted for family size. It restricts properties from being resold to an investor owner within one year of HUD's closing date.

The contract also requires Golden Feather to include a land use restriction addendum with each sales contract and place the restrictions in the deed in order to provide a written record that the organization has agreed to the resale restrictions. The addendum restricts the nonprofit organization from reselling the property for an amount in excess of 110 percent of the net development costs.

Restriction addendum not executed or recorded.

Golden Feather's Contract Department manager said land use restriction addendums were not executed or forwarded to the closing agent. The manager said the Homeownership Center told her the addendum was not required. However, after Golden Feather officials researched the issue they believe they misinterpreted the instruction. A review of property records maintained by Golden Feather confirmed the absence of executed land use restriction addendums.

Golden Feather's Closing Department manager said land use restriction addendums were not included with documents submitted by the closing agent. The

Finding 2

closing agent verified the addendums were not recorded.

Indications of program abuse.

To illustrate the effect of omitting the land use restriction addendum, Table 1 below presents 11 property transactions that may have exceeded the restriction amount or may not have been sold as a principal residence. This is not a comprehensive list and is for illustration purposes only.

For example, six properties were transferred to a trust, which subsequently sold the properties for amounts ranging between 228 percent and 446 percent greater than the HUD discounted amount. Three properties were sold to the same buyer who subsequently resold the properties within six months for amounts ranging between 196 percent and 597 percent greater than the HUD discounted amount. Two properties were resold by the nonprofit organization on the same day they purchased the properties from HUD. The properties were subsequently resold within six months for 177 percent and 251 percent greater than the HUD discounted amount.

Table 1 Indications of Program Abuse

FHA Case No.	HUD Closing Date	Discount Purchase Amount	Non Profit ID	Resale 1 Date Deed Signed	Buyer ID	Resale 1 Sales Amount	Resale 2 Date Deed Signed	Resale 2 Sales Amount	Percent Over Discount Amount
131-691429	12/23/99	\$39,550	CWCS	12/22/99	CRNL	\$48,500	03/31/00	\$70,000	177
131-799365	11/22/99	\$28,000	GSF	11/22/99	15687	\$0	03/13/00	\$125,000	446
131-345889	01/04/00	\$37,800	GSF	01/04/00	15687	\$0	02/23/00	\$86,000	228
131-687880	10/18/99	\$28,000	CWCS	10/18/99	AB	\$36,000	03/28/00	\$55,000	196
131-771813	12/17/99	\$23,100	CWCS	12/17/99	AB	\$33,000	03/09/00	\$138,000	597
131-824009	10/08/99	\$39,200	CWCS	10/08/99	AB	\$48,500	12/21/99	\$122,000	311
131-646815	12/23/99	\$49,000	CWCS	12/23/99	JO	\$58,500	03/22/00	\$123,000	251
131-634381	11/24/99	\$18,200	GSF	12/02/99	15687	\$0	02/16/00	\$71,000	390
131-807848	01/28/00	\$23,100	GSF	02/02/00	15687	\$0	03/13/00	\$69,500	301
131-456334	02/04/00	\$32,480	GSF	02/20/00	15687	\$0	03/21/00	\$90,000	277
131-788238	01/13/00	\$21,000	GSF	01/24/00	15687	\$0	04/10/00	\$61,000	290

Note: A buyer ID with a two-letter designation denotes an individual, a four-letter designation denotes an organization and a buyer ID number denotes a trust.

Auditee Comments

Excerpts from Golden Feather's comments follow. Appendix B contains the complete text of the comments.

When Golden Feather assumed responsibility, the inventory had swelled to an unprecedented 5,800 homes in the four state region. Many buyers were frustrated and delayed in their efforts to close as each file had to be analyzed to assure that the same property was not awarded to more than one party. During this transition period, HUD permitted Golden Feather to dispense with the requirement of a Land Use Restriction Addendum on qualified nonprofit sales.

In the course of the transition, this direction was never countermanded and, accordingly the Land Use Restriction Addendum was not added to the list of required documents until July 2000.

The Contract does not include a sample addendum and a search of the available forms on HUD's web site yields only the addendum applicable to Officers and Teachers. The form that Golden Feather is using is adapted from the HUD Handbook but even this form does not include all of the restrictions referenced in this report.

The Addendum itself is not a recorded instrument and does not provide any additional protection to HUD beyond that which is already provided by HUD's annual nonprofit reporting requirements.

**OIG Evaluation of
Auditee Comments**

We disagree that HUD permitted Golden Feather to dispense with the use of the Land Use Restriction Addendum. Atlanta Homeownership Center officials confirmed that the Land Use Restriction Addendum was required and the requirement was not waived. The contract requires Golden Feather to include a Land Use Restriction Addendum with each sales contract and place the restrictions in the deed in order to provide a written record that the organization has agreed to the resale restrictions. HUD did not execute a contract modification or

amendment dispensing with the use of the Land Use Restriction Addendum.

We also disagree that the Addendum does not provide any additional protection to HUD beyond that which is already provided by HUD's annual nonprofit reporting requirements. Table 1 illustrates the type of abuse that may have been discouraged or prevented if the Addendums were executed and recorded. For example, the individuals that purchased properties from the nonprofit organizations may not have purchased the properties had they been aware of the restrictions.

Golden Feather's statement that the Addendum itself is not a recorded instrument is not entirely correct. The contract requires Golden Feather to place the restrictions in the deed in order to provide a written record that the organization has agreed to the resale restrictions. The Addendum itself could be recorded to satisfy the requirement. The restrictions must be recorded.

Recommendations

We recommend that the Director of the Atlanta Homeownership Center:

- 2A. Assures that Golden Feather executes a land use restriction addendum with each sales contract and records the addendum with the deed.

Properties Not Maintained

Golden Feather did not preserve, protect and maintain HUD owned properties. Golden Feather's inspectors did not always identify and report deficiencies and did not always correct reported deficiencies. OIG's inspectors identified 92 deficiencies at 22 of 26 properties they inspected. Golden Feather's inspectors reported 33 deficiencies with 16 of the 26 properties. The Contract Manager and Assistant Vice President and Manager of the Property Management Department attribute the difference to poor inspections. The Assistant Vice President said 50 percent of the time inspectors just open and close the door. The officials attribute the lack of corrective action to a high turnover in the Work Order Department, a lack of training and employees not properly identifying deficiencies and writing work orders. Because property conditions were not properly maintained, the health and safety of neighbors and potential buyers were threatened and property marketability was impaired. OIG's site inspections results are contained in Appendix A.

Contract requires properties to be protected, preserved and maintained.

Section C-2 of the contract requires Golden Feather to routinely inspect and take all actions necessary to preserve, protect, and maintain each property in a presentable condition at all times.

This includes correcting any conditions that present a health or safety hazard to the public within 24 hours of discovery. Repairing broken steps or floorboards, removing hazardous material such as gasoline cans, oil-soaked rags, dead animals and feces. Securing the property to prevent unauthorized entry using a locking system. Removing and properly disposing of all interior and exterior debris both after property conveyance and on a continual basis. Maintaining the lawn, shrubbery and trees consistent with neighborhood standards. Protecting the property from damage from the elements, through such measures as repairing broken windows, patching roof leaks, and replacing functional shutters. Repairing all damages due to vandalism such as broken windows, spray paint to the exterior or interior of the home, and theft of appliances. Exhibit 15 of the contract requires inspectors to determine whether defective paint surfaces exist.

Controls over property inspections and correcting deficiencies were weak.

Management controls over the inspection process were weak. Golden Feather's Vice-President of the Property Management Department said controls

over the inspection process consisted of re-inspecting 10 percent of the inventory using senior level inspectors. The officials also said the re-inspection results were used to provide discussion topics for weekly inspector training classes and assess inspector's performance. However, Golden Feather was unable to produce any documents to support the existence of the re-inspection program or its results.

Golden Feather recognized the need to improve the quality of its re-inspection program in June 2000. The improved re-inspection program consisted of re-inspecting 20 percent of the property inventory using senior level inspectors. The re-inspection results were used to provide discussion topics for weekly inspector training classes and assess inspector's performance. Golden Feather produced a report confirming approximately 17 percent of the properties were re-inspected in July 2000. However, this was after OIG conducted its inspections. Therefore, we did not test the control.

Management controls over correcting reported deficiencies were weak. Golden Feather's Vice President of the Property Management Department said controls over correcting reported deficiencies consisted of reviewing between ten and 20 work orders per day to determine if corrective action was taken. However, Golden Feather was unable to produce any documentation to support the existence of the verification process or its results.

Health and safety hazards.

Health and safety hazards were present in 14 properties we inspected. OIG's inspectors identified health hazards such as a dead pigeon in the kitchen of one property and a dead cat in the basement of another. The inspectors identified safety hazards such as broken steps and floorboards at all four properties. The contract specifically identifies dead animals, broken steps and floorboards as hazards.

OIG's inspectors also identified other hazardous conditions that were not specifically identified in the contract. These conditions included broken glass, rusty nails protruding upward, missing stair

railings on a second floor deck, a ceiling and a roof overhang near collapse, loose chimney bricks on the roof ready to fall to the ground and uncovered electrical boxes.

Golden Feather's inspectors reported two hazardous conditions. The contract manager said the remaining deficiencies were not always reported due to inspector oversight.

A review of deficiencies reported by Golden Feather's inspectors disclosed that deficiencies were not always corrected. For example, on May 18, 2000, Golden Feather's inspectors reported a dead cat in the basement at property 131-536752. On June 8, 2000, OIG's inspectors identified a dead cat in the basement. Golden Feather had not issued a work order to correct the deficiency as of August 7, 2000. The contract manager said a work order should have been written the first time the dead cat was reported.

Properties were not secured.

Eight properties were not properly secured to prevent unauthorized entry. Properties had opened windows, unlocked or missing locks and keys left in keyholes or under a mat. Three of the eight properties had been vandalized.

Golden Feather's inspectors reported one improperly secured property. Golden Feather took corrective action approximately two months after its inspectors reported the deficiency. The contract manager said missing locks and keys left in doors or under mats were due to realtors that did not lock the doors.

Debris was not removed and lawns were not maintained.

Physical appearances were not maintained by removing debris or maintaining lawns. OIG's inspectors identified 13 properties with debris and 16 properties without lawn maintenance. The debris included washers and dryers, trash, clothing, toys, wood, and a fallen tree. Grass had reached over two feet high at one property. Picture number one below evidences the lack of lawn maintenance.



Picture Number 1. Evidence of the lack of lawn maintenance at property 131-852341.

Golden Feather’s inspectors reported debris at four properties and deficient lawn conditions at 13 properties. Golden Feather’s inspectors did not report the remaining debris or lawn maintenance deficiencies due to inspector oversight.

A review of deficiencies reported by Golden Feather’s inspectors disclosed that deficiencies were not always corrected. For example, Golden Feather’s inspectors reported debris at property 131-852341 on May 23, 2000 and again on June 13, 2000. OIG’s inspectors identified debris on June 6, 2000. Golden Feather had not issued a work order to remove the debris as of August 7, 2000. Officials believe that a high turnover in the Work Order Department contributed to the oversight. We were unable to determine if corrective action was taken for deficient lawn maintenance due to the lack of an audit trail.

Properties were not protected from the elements.

Properties were not protected to prevent damage from the elements or further deterioration. OIG inspectors identified nine properties with broken window glass and 11 properties with indications of roof leaks.

Golden Feather's inspectors reported broken window glass at four properties and roof leaks at three properties. Picture number two below evidences a roof leak.



Picture Number 2. Evidence of a roof leak in the common hall ceiling at property 131-888615.

A review of deficiencies reported by Golden Feather's inspectors disclosed that deficiencies were not always corrected. For example, Golden Feather's inspectors reported a roof leak at property 131-888615 on May 9, 2000. OIG's inspectors identified a roof leak on June 7, 2000. Golden Feather had not issued a work order to repair the leak as of August 7, 2000. The contract manager said it appears that someone in the Work Order Department missed the problem and did not write a work order.

Vandalism was not repaired.

Golden Feather did not repair damage caused by routine vandalism at seven properties. The vandalism included graffiti, missing kitchen cabinet doors, missing kitchen plumbing and bathroom plumbing fixtures. Golden Feather's inspectors reported vandalism at one property and took

Defective paint surfaces were present.

corrective action. The remaining deficiencies were not reported due to inspector oversight.

Defective paint surfaces were identified at 14 properties. The defects consisted of cracking, scaling, chipping and peeling paint.

Golden Feather's inspectors reported defective paint at five properties. The contract manager said their inspectors should have inspected and reported all defective paint surfaces.

A review of deficiencies reported by Golden Feather's inspectors disclosed that deficiencies were not always corrected. For example, Golden Feather's inspectors reported defective paint at property 131-836686 on May 16, 2000 and again on May 22, 2000. OIG's inspectors identified defective paint on June 7, 2000. Golden Feather had not issued a work order to correct the deficiency as of August 7, 2000.

Auditee Comments

Excerpts from Golden Feather's comments follow. Appendix B contains Golden Feather's the full response.

The condition of the HUD inventory in this area is better than it has been in years, Golden Feather's procedures have been instrumental in this turn-around. This report gives a false sense of the condition of the inventory because it has no baseline from which to compare. It simply chose 26 properties from an inventory of 3,500 and concluded from this non-representative sample that Golden Feather did not preserve, protect and maintain HUD owned properties. This conclusion is overreaching given the data sampled and fails to compare the condition of the inventory today against what it was when Golden Feather took over ten months earlier.

In June 2000, Golden Feather implemented a comprehensive inspector grading program which requires quality control inspectors to follow behind routine inspectors to review their work. This report

is critical of Golden Feather's inspection quality control prior to June 2000, not because the program was ineffective, but solely because Golden Feather did not produce documents to support it. The documents to verify the effectiveness of Golden Feather's prior re-inspections program are actually the inspection reports themselves. They are available in the files the Office of Inspector General had access to for four months. To ask Golden Feather to spend numerous hours segregating these documents from the files is neither reasonable nor a requirement of the Contract. The fact that Golden Feather did not produce these documents does not mean they do not exist nor does it mean the program was ineffective. To the contrary, they exist and have been available to the Office of Inspector General during its entire audit.

Golden Feather strongly disagrees with the finding that management controls over correcting reported deficiencies were weak. Golden Feather's internal system, REAM, carefully tracks work order assignments and reports are run daily and weekly for management to track status and trends. Examples of many of these reports were provided. The example of a control cited is only one of many and the report's inference that it is the only such control is misleading and presents an inaccurate representation of Golden Feather's systems and procedures.

The statement in the introductory paragraph of this finding, "The Assistant Vice President said 50 percent of the time inspectors just open and close the door.", is false and Golden Feather denies not only the veracity of the statement but also that this statement was ever made. If it were true, then the sign-in sheets inside HUD Homes would not have Golden Feather inspection sign-ins which correspond with the written inspection reports. The truth is that the sign-in sheets and the inspection reports do correspond thereby evidencing that in fact, the statement attributed to the Assistant Vice President was untrue.

OIG Evaluation of
Auditee Comments

We disagree with Golden Feather's statement that the report gives a false sense of condition of the inventory. The audit disclosed that Golden Feather failed to meet its contractual obligation to preserve, protect and maintain 22 of 26 HUD owned properties. The contract does not provide for a baseline comparison when determining if Golden Feather preserved, protected and maintained properties.

We also disagree with Golden Feather's statement that the 26 properties were non-representative. The sample was randomly selected without bias. The sample size was not determined with the intention of extrapolating the inspection results. However, the sample size was sufficient to determine that Golden Feather had material management control weakness in the way it manages all of HUD's properties.

Golden Feather's comments that we found inspection quality control ineffective solely because Golden Feather did not produce documents is inaccurate. We determined that management controls over property inspections were weak based on a comparison of inspection results between OIG's inspectors and Golden Feather's inspectors and a review of Golden Feather's management controls over the inspection process. OIG inspectors identified 92 deficiencies at 22 of 26 properties inspected. Golden Feather inspectors identified 33 deficiencies at 15 of the 26 properties. Golden Feather reported that it re-inspected properties in order to maintain quality over its inspection process. We concluded that the difference between the inspections indicated the re-inspection process had weaknesses. The lack of documentation to support Golden Feather's procedures is another indication of a control weakness.

Golden Feather further stated to spend numerous hours segregating inspection documents from the files in order to demonstrate that an inspection quality control program was neither reasonable nor a requirement of the Contract. We disagree, Golden

Feather was contractually obligated to identify all inspections conducted and all corrective actions taken and ensure records were available to HUD personnel throughout the term of the contract.

We disagree that management controls ensured reported deficiencies were corrected. A comparison of Golden Feather's inspection reports to work order reports disclosed that deficiencies were reported and work orders were not issued. Golden Feather's employees agreed that deficiencies were not always corrected and work orders should have been written and deficiencies corrected. Officials also believed that oversights were due to a high turnover in the Work Order Department. Golden Feather's Vice President of the Property Management Department told us that the controls in place consisted of reviewing work orders to determine if corrective actions were taken. When we asked for documents that would support the work order review, Golden Feather did not have any documentation. The lack of documentation does indicate a weak management control structure.

We believed the Assistant Vice President and Manager of the Property Management Department was accurate when he stated 50 percent of the time inspectors just open and close the door. We disagree with Golden Feather's response that inspection sign-in sheets correspond with the written inspection reports thereby evidencing the statement 50 percent of the time inspectors just open and close the door was false.

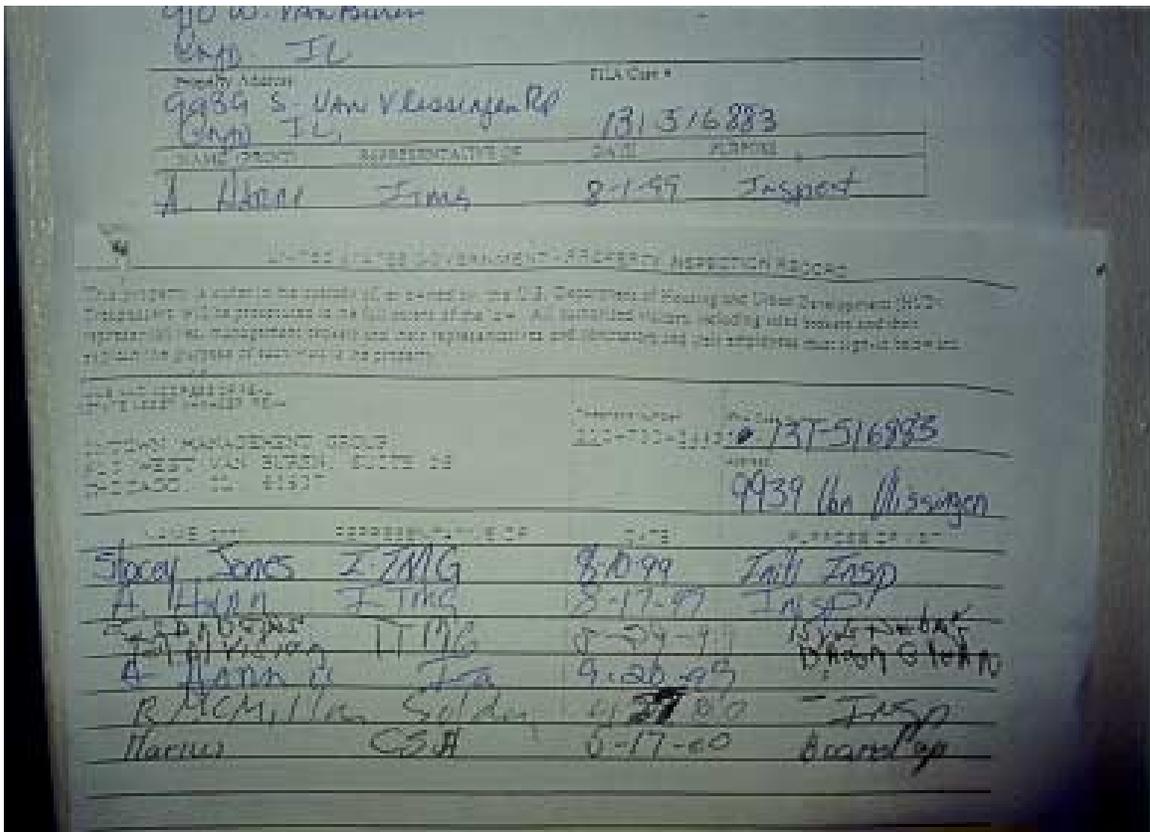
In fact inspection sign-in sheets do not correspond with the written inspection reports. For example, a comparison of inspection records and the sign-in sheet for property 131-516883 disclosed that Golden Feather's inspectors claimed to inspect the property five times between April 7, 2000 and May 29, 2000. The sign-in log supports only one inspection on April 27, 2000. The second entry represents a board up visit. The remaining entries represent prior contractor activity. Table 2 below compares the inspection dates with the dates on the

Finding 3

sign-in sheet. Picture number three below evidences one physical property inspection.

Table 2 – Comparison of Inspection Reports to Sign-In Sheet.

Date of Inspection Report	Date on Sign-In Sheet	Purpose of Visit
	8/10/99 to 9/20/99	Prior Contractor
4/07/00		
4/27/00	4/27/00	Inspection
5/10/00		
	5/17/00	Board-up
5/23/00		
5/29/00		



Picture Number 3. Inspection Record at Property 131-516883.

Recommendations

We recommend that the Director of the Atlanta Homeownership Center:

- 3A. Assures that Golden Feather corrects the maintenance deficiencies identified by our inspectors.
- 3B. Assures that Golden Feather develops and implements procedures for the oversight of inspections.
- 3C. Assures that Golden Feather takes corrective action on deficiencies reported by Golden Feather's inspectors.

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Unapproved Appraisers used for HUD Properties

Golden Feather did not always use appraisers that were listed on HUD's Lender Selection Roster. Golden Feather's Vice President believed HUD-approved supervisory appraisers could supervise the unapproved appraisers. However, after researching HUD's policies, the Vice President determined that Golden Feather would require all appraisers to be listed on HUD's Roster. Because unapproved appraisers were used, HUD's risk in obtaining an inaccurate list and sales price has been increased.

Approved Appraisers are Required.

Exhibit 1 of the contract requires Golden Feather to ensure that each appraiser has a State designation that meets the minimum criteria of the Appraisal Qualifications Board. The contract also requires that appraisers be listed on HUD's Lender Selection Roster.

HUD Handbook 4150.2 requires that all appraisers be state licensed or certified, pass a HUD test on appraisal methods and reporting and pass a background check.

Controls over the Verification Process were Weak.

Golden Feather's management controls did not ensure appraisers were listed on HUD's Lender Selection Roster. If an appraiser was not listed on the Roster, Golden Feather would request a copy of the appraiser's professional license from the appraiser's employer. If the appraiser was licensed and their supervisor was listed on the Roster, Golden Feather would accept the appraisal.

As of August 2000, Golden Feather required all appraisers to be listed on the Roster. The change in policy was implemented after our review. Therefore, we did not test the new policy.

Appraisers were not always listed on the Roster.

Four appraisal companies appraised 213 properties using seven unapproved appraisers. Officials from the four companies said they believed that a HUD-approved supervisory appraiser was allowed to sign off on the work of a licensed appraiser. All of the appraisers were state licensed.

Finding 4

Approved Supervisors did not always Review Work.

The unapproved appraisers were not always supervised. A review of 21 appraisals, three appraisals from each of the seven unapproved appraisers, disclosed HUD-approved supervisory appraisers did not always sign the appraisals or physically inspect the property.

Auditee Comments

Excerpts from Golden Feather's comments follow. Appendix B contains the complete text of the comments.

A review of the Contract language clearly demonstrates the ambiguity in this issue. Before explaining the contractual ambiguities, Golden Feather wishes to clarify a statement in the report's introduction to this finding. The report states that Golden Feather elected to require all appraisers to be on the Roster after "researching HUD policies." This statement is not complete. In fact, Golden Feather does not concede that the Contract requires the exclusive use of Roster appraisers. Golden Feather contends that this issue is not clearly answered by either the Contract or the HUD Handbook. Golden Feather elected to use Roster appraisers in an attempt to eliminate any potential problems that a buyer might encounter attributable to the ambiguity of this issue (and out of respect for the Atlanta Homeownership Center's directive on the issue).

OIG Evaluation of Auditee Comments

We disagree with Golden Feather's statement that a review of the contract language clearly demonstrates the ambiguity in this issue. Exhibit 1 of the contract states appraisers must be on the HUD Lender Selection Roster, which is maintained by the Homeownership Center. Section C-3 of the contract states where handbooks, notices, or instructional memorandums or letters conflict with the provisions of this contract, the provisions of this contract shall control.

Additionally, HUD-approved supervisory appraisers did not always physically inspect the property. This practice is unacceptable under all appraisal rules.

Recommendations

We recommend that the Director of the Atlanta Homeownership Center:

- 4A. Assures that Golden Feather uses only HUD-approved appraisers listed on the Lender Selection Roster.
- 4B. Assure that Golden Feather obtain a new appraisal, by an independent approved appraiser, for the insured properties currently in inventory the seven unapproved appraisers appraised.
- 4C. Assure that HUD property owners did not pay an inflated amount due to unapproved appraisers. If HUD property owners paid an inflated amount, refund the overpayment.

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Untimely Appraisals and Disposition Programs

Golden Feather experienced processing delays with appraisals and disposition programs. Eleven of the 29 properties we tested were delayed at various stages due to employee oversight, mistakes and policies that were inconsistent with HUD's requirements. Because properties remained in inventory longer, HUD could have incurred an increase in holding costs and increased the possibility of property deterioration.

Golden Feather is Responsible for Marketing Properties Timely.

The contract requires Golden Feather to obtain an appraisal of each property's current value no later than ten business days after HUD obtains title to the property. Properties assigned within 90 calendar days from the date of the Phase II transition, extends the period to 15 days.

Handbook 4310.5, REV-2 requires that Golden Feather complete, review and approve the disposition program within three business days of receipt of the appraisal.

Receipt of Appraisals were Not Always Timely.

Golden Feather did not always appraise properties timely. Four of 29 properties were appraised from six to 56 days late. The contract manager said one appraisal was delayed because the property was occupied, two were returned to the appraisers for corrections and the remaining one was just late.

Golden Feather's controls consisted of recording the acquisition date and the date the appraisal was completed in the Real Estate Asset Management system. Officials said exception reports were reviewed weekly and appraisers were contacted on the eighth-business day if appraisals had not been received. Even though management controls appeared to be sufficient, the controls did not prevent untimely appraisals. We were unable to determine why appraisals were untimely due to the lack of an audit trail.

Golden Feather was unable to provide any records to document exceptions, monitoring, phone conversations or discussions regarding the

Disposition Programs
Not Always Approved
Timely.

identification and corrective action taken for untimely appraisals.

Golden Feather did not always approve property disposition programs timely. Nine out of 29 properties were approved from one to 50 days late. Golden Feather was unaware of HUD's requirement to approve disposition programs within three business days of receipt of property appraisals. The contract manager said delays might have occurred because Golden Feather's policy was to approve disposition programs once a week.

However, five of the nine properties were delayed more than four days, which was inconsistent with Golden Feather's once a week policy. The contract manager attributed three of the five delays to circumstances related to the start-up period. Officials would not comment on the remaining two delays.

Missing Inspection
Reports

We were unable to determine if Golden Feather performed initial inspections timely for three of 29 property inspections. Initial inspection reports were missing. The contract manager attributes the missing records to filing errors.

Auditee Comments

Excerpts from Golden Feather's comments follow. Appendix B contains the complete text of the comments:

The Office of Inspector General's review of a small sample of the homes sold in the last year overlooks this broader perspective and does not provide an appropriate overview of the program's success to date.

Unfortunately, the report is devoid of any specific or identifiable case data, making it impossible to comment discretely on the origin of the individual findings. Additionally, these findings do not appear to account for the external forces affecting the practical application of the contract.

The existence of delays is primarily a result of external factors. Golden Feather's internal controls identify these delays and enable Golden Feather staff to take appropriate remedial action to redress delays as they are encountered.

The finding that "Golden Feather did not always appraise properties timely" is troublesome in light of the contributing causes, which may delay the anticipated delivery of appraisals. There are a multitude of external factors that may surface.

The report contends that appraisals should be completed within ten business days "after HUD obtains title to the property." This approach, however, ignores the realities of property conveyance under the M&M program. GFR usually has no means of knowing when a property will come into its inventory other than the receipt of the electronic conveyance. Accordingly, until GFR receives the conveyance and enters it into the system, it cannot order its appraisal. It should also be noted that the Contract itself does not call for appraisals to be completed within ten days of HUD's acquisition of the property. To the contrary, the Contract requires that appraisals be obtained within ten business days of "assignment" of the property (M&M Contract, Section C-2, IV). It should be noted that there is an internal contradiction within the Contract that makes the commencement date for the appraisal timeframe unclear. Section C-2, V, Paragraph-9. Since it would be impossible to achieve contract compliance with the ten-day period commencing with HUD acquisition, Golden Feather bases its timeframe calculation on the assignment date as provided by the Contract.

The report contends that Golden Feather "did not always approve property disposition programs timely". This finding fails to consider the environment in which the sales disposition program operates and the external variables that interfere with the smooth transition from appraisal to listing.

The report, relying by reference on the HUD Property Disposition Handbook 4310.5, Rev 2, is critical of Golden Feather's property disposition program in those cases where a disposition has not been approved within three days of receipt of appraisal. This criticism, however, is based on requirements that significantly predate the existence of the Marketing and Management program and once again ignores the presence of external factors.

OIG Evaluation of
Auditee Comments

We disagree with Golden Feather's statement that the small sample of homes sold overlooks the broader perspective and does not provide an appropriate overview of the program's success to date. The sample was randomly selected without any bias. The sample size was not determined with the intention of extrapolating the results. However, the sample size was sufficient to determine that Golden Feather had material management control weakness in the way it manages the timeliness of appraisals and disposition programs for all of HUD's properties.

We disagree that Golden Feather did not have the opportunity to comment on each case. On July 11, 2000, we discussed all of the untimely properties located in Chicago, Illinois with Golden Feather's Contract Manager and Manager of the Listing Department. On July 12, 2000, we discussed all of the untimely properties located in Indianapolis, Indiana with Golden Feather's Contract Manager and Marketing Director. On August 17, 2000, we conducted follow-up discussions about untimely disposition programs with Golden Feather's Contract Manager and Manager of the Listing Department. Golden Feather refused to comment on several untimely disposition properties when asked on August 17, 2000.

We also disagree that the existence of delays is primarily a result of external factors. Golden Feather is required to process appraisals and disposition programs within prescribed timeframes. It is Golden Feather's responsibility to ensure that appraisers comply with the timeframes prescribed in the contract.

Exhibit 1 of the contract states that upon receipt of notice of a Mortgagee's assignment of a property for listing or transfer Golden Feather shall obtain an appraisal for such property within ten business days. Our analysis gave the contractor the benefit by using the date Golden Feather received HUD Form 27011A from the mortgagee instead of the date HUD electronically notified Golden Feather of the assignment. Under both scenarios, Golden Feather obtained untimely appraisals.

We disagree that Golden Feather is not required to comply with HUD Property Disposition Handbook 4310.5, Rev 2. Section C-3 of the contract requires Golden Feather to comply with the National Housing Act, HUD regulations, notices, handbooks, instructional memorandums and letters.

Recommendations

We recommend that the Director of the Atlanta Homeownership Center:

- 5A. Assures that Golden Feather develops and implements controls that will allow them to process appraisals and disposition programs within the required time frames.

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Management Controls

In planning and performing our audit, we considered Golden Feather’s management controls as they related to the ongoing management and marketing of acquired properties in order to determine our auditing procedures, not to provide assurance on management controls. Management controls include the processes for planning, organizing, directing and controlling program operation. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Management Controls

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

- Program Operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Validity and Reliability of Data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with Laws and Regulation – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding Resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss and misuse.

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

Significant Weaknesses

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

- Program Operations

Golden Feather’s management controls did not always ensure compliance with HUD policies or

with the management and marketing contract. For example:

1. Restrictions were not executed or recorded which prohibited nonprofit organizations from: 1) purchasing properties at a 30 percent discount and reselling them for more than 110 percent of cost; and 2) selling the discounted properties to parties that did not intend to occupy them as a principal residence.
2. Properties were not inspected properly and reported deficiencies were not always corrected.
3. Approved appraisers were not always used to appraise HUD properties.
4. Property appraisals and disposition programs were not always timely.

- Safeguarding Resources

Golden Feather's management controls did not reasonably ensure compliance that resources were safeguarded against fraud, loss and misuse. Due to the lack of separation of duties and supervisory oversight, a Golden Feather employee was able to solicit a kickback from two appraisers in exchange for increased work assignments.

Follow Up On Prior Audits

This is the first audit of Golden Feather Realty Services, Incorporated for the Atlanta Homeownership Center Area A-1 by HUD's Office of Inspector General.

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Results of OIG Site Inspections of Chicago and Indianapolis Properties

No	FHA Case No	Health & Safety Hazard	Property Secured	Debris	Lawn Cut	Broken Window	Roof Leaks	Vandalism	Defective Paint
Chicago									
1	131-798360			X			X		X
2	131-888615	X				X	X	X	X
3	131-821372	X		X		X	X	X	X
4	131-516883	X	X	X	X		X	X	X
5	131-333337			X	X	X	X	X	
6	131-704534	X		X	X				X
7	131-536752	X				X		X	X
8	131-919709	X	X	X	X	X	X		X
9	131-852341	X	X	X	X				X
10	131-836686		X	X	X	X			X
11	131-805019	X	X		X			X	
12	131-680016			X	X	X	X		X
	Subtotal	8	5	9	8	7	7	6	10
Indianapolis									
13	151-502747								
14	151-502396		X		X			X	
15	151-448611	X		X	X				X
16	151-539745	X		X	X		X		X
17	151-430244				X				X
18	151-504115		X		X	X			
19	151-508887								
20	151-507382	X			X				
21	151-412771								
22	151-529349	X	X		X				
23	151-492738	X		X			X		
24	151-537803			X	X	X	X		
25	151-459927								
26	151-463504	X					X		X
	Subtotal	6	3	4	8	2	4	1	4
	Total No. of Deficiencies	14	8	13	16	9	11	7	14
	Deficiencies Identified by Contractor	2	1	4	13	4	3	1	5
	Deficiencies NOT Identified by Contractor	12	7	9	3	5	8	6	9

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Auditee Comments

ACQUISITIONS DEPARTMENT AND CONTRACTOR OVERSIGHT

Auditee
Comments

GFR acted swiftly
and resolutely and
thereby prevented
any potential loss
to HUD or GFR

Golden Feather Realty Services' ("GFR") internal controls are comprehensive and have recently been strengthened to address potential business abuses by employees or contractors. No controls, however, regardless of their breadth, can prevent every potential act of deception, especially if committed by a trusted employee. In the case of GFR's former New Acquisitions manager, even the most stringent controls (and an adoption of the very recommendations contained in the OIG Report), would not have *prevented* this manager's conduct. In addition, it must also be noted that GFR's existing controls were sufficient to discover the wrongful act *before* a kickback was paid and *before* any influence was exerted. GFR acted swiftly and resolutely to take corrective action while always maintaining open communication with HUD. Because of the early detection and rapid response, neither HUD nor GFR was victimized by this employee's conduct. In fact, it should be noted that all appraisal expenditures are GFR's expenses. HUD does not pay for these appraisals nor does HUD reimburse GFR for these expenses. Accordingly, at no time was there ever any risk of loss to HUD in this matter. Finally, contrary to the statements made above in the OIG's report, the Office of the Inspector General *was* notified of this issue by the Director of the Atlanta HOC immediately upon discovery of the alleged conduct and the OIG was aware of the matter four days prior to the employee's dismissal.

GFR's controls assure that key duties in authorizing, reviewing and paying for contractors' work (including appraisers) are separated among different individuals and different offices. We disagree with the OIG's finding that the responsibilities of selecting appraisers and issuing work orders must be separated. In the case of appraisal ordering, the department manager (or an employee under her direct control) orders appraisals from existing contractors (already approved by management other than the person issuing the work) based on territories. These orders are reviewed weekly by the Contract Manager as part of GFR's Weekly Matrix Report (which contains a complete report of every appraiser and the status of his or her work). The Contract Manager, should he detect an unusual variation in ordering

patterns, would then investigate to assure that aberrations in volume are justified. The Weekly Matrix Report is also independently reviewed by GFR's senior management who may also institute an investigation into any unusual change in the prior order history.

GFR also works closely with its contractors to explain its zero tolerance policy and encourage them to contact senior management if they encounter inappropriate behavior from a GFR employee. The fostering of these relationships is among the most effective controls for discovering untoward conduct from an employee. In the case of the former New Acquisitions Department manager, the employee was alleged to have solicited a kickback from two appraisers. Both appraisers reported this conduct immediately (one reported to GFR and the other reported to the Atlanta HOC). Because of these reports, HUD and GFR were able to act together to prevent any loss.

GFR's internal and external controls pose a formidable deterrence to procurement abuse.

In addition to these existing controls, effective August 1, 2000, GFR implemented its Contractor Maintenance Control Plan (the "CMCP") which is a comprehensive policy statement, action plan and audit control specifically designed to detect and prevent potential business abuses by employees or contractors. The CMCP has been distributed to all managers, employees who serve in a procurement capacity, and to all contractors providing services related to HUD Homes. GFR is confident that its existing segregation of duties, its internal controls, and the CMCP form a formidable set of internal and external controls to address the possibility of procurement abuse. These controls, all implemented prior to the release of the OIG's draft findings, address and exceed the recommendations contained therein.

The claim of a potential solicitation of payment was reported to the OIG by the Director of the Atlanta HOC immediately upon its discovery and GFR was apprised of this report at the same time it first learned of the allegation (four days prior to the employee's dismissal). Once aware that the OIG was involved, it would have been superfluous for GFR to make a second report to the same department.

The intent of Section 52.203-07 of the Federal Acquisition Regulations is to assure that the OIG is made aware of potential violations. In this instance, the intent of this

regulation was unquestionably fulfilled as the alleged violation was reported to the OIG promptly upon its discovery.

The OIG was made aware of the potential violation four days before GFR dismissed the employee

Upon receiving a second report from a contractor, GFR terminated the employee, with notice to, and approval from, the Director of the Atlanta HOC. Any further delay at the point would have subjected GFR to potential financial loss.

No controls, regardless of their reach, can *guarantee* that a rogue employee or contractor will not attempt to gain pecuniary advantage in violation of GFR's policies. Much like a criminal intent on robbing a bank, one can work diligently to deter the wrongful conduct by setting up controls, but, in the end, some individuals may choose to commit the act anyway. For these people, where deterrence and prevention is ineffective, systems must be in place to effectively detect the conduct and react quickly to minimize loss. In the case of GFR's former manager, this is precisely what happened. His conduct was detected and reported promptly, and employment action taken swiftly, to assure that no loss occurred to HUD or to GFR.

Controls Over Resale Restrictions

When Golden Feather Realty Services (“GFR”) assumed responsibility for Area 1 under the Atlanta HOC, it was presented with an enormous challenge. The predecessor contractor had closed only 556 sales in its seven month term¹ and the transactional backlog was massive. For its first three weeks, GFR was also hamstrung in its efforts by the predecessor contractor’s refusal to release HUD’s files. Once the files arrived, they were in disarray and GFR worked for months to resolve the inestimable number of contract issues presented in the transition.

HUD permitted GFR to dispense with requiring a Land Use Restriction Addendum during the transition from the predecessor contractor.

During this time period, GFR worked closely with HUD and this teamwork was essential in addressing issues never anticipated by the M&M Contract (the “Contract”). The Contract did not anticipate that a new contractor would step in after only seven months nor did it foresee that the inventory would nearly double in that same time frame. When GFR assumed responsibility for the A1 area, the inventory had swelled to an unprecedented 5,800 homes in the four state region. Many buyers were frustrated and delayed in their efforts to close as each file had to be analyzed to assure that the same property was not awarded to more than one party. During this transition period, HUD permitted GFR to dispense with the requirement of a Land Use Restriction Addendum (“LURA”) on qualified non-profit sales.

“Because GFR has been requiring the LURA since June, 2000, long before the release of this report, the OIG Recommendation in this finding is moot.”

In the course of the transition, this direction was never countermanded and, accordingly, the LURA was not added to the list of required documents until July, 2000 when its omission was discovered. Once the omission was discovered, GFR acted immediately to remedy the oversight² but, in so doing, discovered some confusion as to the proper addendum to include.

The Contract states that non-profit organizations purchasing at 30% discounts must include a Land Use Restriction Addendum with each contract. *see* M&M Contract, Exhibit 2-4, (J)(3). The Contract does not,

¹ By comparison, GFR closed 4,818 sales in its first seven months in the same area.

² Because GFR has been requiring the LURA since June, 2000, long before the release of this report, the OIG Recommendation in this finding is moot.

however, include a sample addendum and a search of the available forms on HUD's web site³ yields only the addendum applicable to Officers and Teachers (which GFR has been using since contract commencement). The form that GFR is using is adapted from the HUD Handbook but even this form does not include all of the restrictions referenced in the OIG Report.

The absence of Land Use Restriction Addenda neither prejudiced HUD's ability to take action against non-profits, nor did it cause any actual loss to HUD.

An additional source of confusion in this area derives from the fact that only two of the seven closing agent contracts for the A-1 region contain a requirement for including a restrictive covenant in the deeds they prepare on HUD's behalf. Unfortunately, even in these two contracts, the deed restriction language does not track the restrictions in the LURA or in the M&M Contract.

The Addendum itself is not a recorded instrument and does not provide any additional protection to HUD beyond that which is already provided by HUD's annual non-profit reporting requirements. The Atlanta HOC requires every non-profit organization to submit an REO Direct Sales Annual Report which provides a detailed accounting on each sale and assures that the non-profit is complying with all program requirements including, but not limited to, income restrictions on resale, development and rehabilitation requirements, and types of buyers acquiring these properties. These reports are required to be filed by January 30 of each year for a non-profit organization to maintain its eligibility to participate in the program. Any non-profit that fails to file this report loses its certification to acquire additional houses.

"The Contract neither permits nor requires GFR to police these {non-profit} transactions or make inquiry as to the subsequent dispositions."

The OIG Report includes a table ("Table 1") designed to illustrate examples of non-profit abuses of the existing programs. Two important points should be underscored in connection with this data. First, these are examples of non-profit organizations knowingly abusing the system during the time period *after closing* the sale of a HUD Home. After a sale closes, the Contract neither permits nor requires GFR to police these transactions or make inquiry as to the subsequent dispositions. Second, since these non-profits have already shown themselves predisposed to act contrary to the clearly defined rules of the program, there is no credible evidence to suggest that the inclusion of an

³ Searching "HUD Clips" at http://www.hudclips.org/sub_nonhud/html/forms.htm.

addendum would have resulted in any material change in the outcome of these transactions.

If the non-profits follow the reporting requirements, the data in Table 1 of the OIG Report would be clearly presented in their respective annual reports and, regardless of the presence of an LURA, HUD could investigate and take appropriate action. In short, while the LURA was not included in certain transactions, its absence did not prejudice HUD, or cause it any loss, in any of the cases identified in Table 1.

Property Maintenance

Golden Feather Realty (“GFR”) assumed responsibility for the A-1 region of HUD’s inventory on September 22, 1999. At the time GFR took over, the inventory was in extremely poor condition throughout the area. Discussions with community leaders and the City of Chicago confirmed that, in fact, the inventory had been disappointingly maintained for many years. GFR was presented with the enormous and challenging task of cleaning up an inventory that had suffered from years of deferred maintenance.

GFR introduced unique initiatives in this area to improve property conditions that had a long history of deficiencies.

GFR began this process by applying its existing (and proven) systems to the HUD inventory but, in a short time, some of the unique features of this area’s inventory made it apparent that these procedures would have to be refined to address the poor condition of these properties. For example, at the commencement of GFR’s Contract, more than half of the homes in the greater Chicago area were unsecured. To expedite the securing of these many hundreds of homes, GFR employed several securing teams to follow behind inspectors so that the inventory could be re-secured in days, instead of months.

GFR’s “Hot Zone” Program has been instrumental in improving sales and property conditions in the City of Chicago.

In addition, recognizing the unique problems plaguing vacant homes in the city of Chicago, GFR teamed with local authorities from the Police Department and Buildings Department and developed its unique Hot Zone Program. Under the Hot Zone Program, GFR defined certain areas of the city that have been historically susceptible to rapid property deterioration resulting from such causes as high crime, large numbers of gangs and drug users and increased presence of transients and other adverse occupants. Instead of inspecting these homes twice monthly as is standard under the Contract, GFR is now seeing these homes twice weekly at its own expense. Positive results were seen in under a month. The early progress was seen in the form of vastly reduced complaints from residents and city officials. The more tangible results were seen shortly thereafter as homes in these areas began to sell in unprecedented numbers. When GFR assumed the Contract, the City of Chicago had approximately 1,400 HUD Homes. That number is now below 750 and continues to decline each month. This kind of inventory reduction was only possible because the property conditions improved so that the properties could become marketable again.

GFR was awarded a “Best Practices” Award by HUD for its efforts in its first year in Illinois.

In addition to unique inspection and maintenance initiatives, GFR embarked on an ambitious program to reach out to the communities as part of its efforts to improve property conditions. While the M&M Contract (the “Contract”) envisions community outreach in relation to the sales of properties, GFR, on its own and in conjunction with HUD, went far beyond the Contract in an attempt to repair HUD’s tattered image. GFR has partnered with towns and villages, with city leaders and with neighborhood activists, all in an effort to improve the condition of the homes in their neighborhoods. These leaders, and their constituencies, have become GFR’s eyes and ears in their neighborhoods. GFR’s senior management has spent dozens of hours meeting with community and municipal leaders and listening to the concerns that have intensified over many years. Given the historically poor condition of the properties, GFR’s initial assurances that conditions would improve quickly were met with understandable skepticism. The results, on the other hand, have been met with acclaim from these same leaders. For example, (Name Removed), Executive Director of the National Training and Information Center, has been extremely supportive of GFR’s efforts in its first year, recognizing GFR’s substantial improvement in the management of HUD REO properties.

All of these efforts were instrumental in improving the condition of the HUD inventory and making these homes more marketable. GFR’s initiatives in the state of Illinois (and the resulting reduction in inventory) were acknowledged nationally with the awarding of a HUD “Best Practices” Award in the Summer of 2000.

GFR has collected hundreds of thousands of dollars this year on mortgagee neglect claims for HUD.

GFR was also faced with an area that had suffered from years of mortgagee neglect. Despite the strong opposition posed by many mortgagees, GFR has collected hundreds of thousands of dollars this year on mortgagee neglect claims for HUD. In addition, and more importantly, now that the mortgage community knows that GFR is pursuing these claims, the instances of mortgagee neglect are beginning to decline. This reduction means properties are conveyed to HUD in better condition than they had been for many years, thereby making the properties more likely to sell quickly and for a greater return to the mortgage insurance fund.

Do the improvements of the preceding ten months mean that the entire mountain has been scaled? No, far from it. Years of deferred maintenance will not be fixed in ten months. It is, however, critical to note that the condition of the HUD inventory in this area is better than it has been in years, and GFR's procedures have been instrumental in this turn-around.

The condition of the HUD inventory in this area is better than it has been in years, and GFR's procedures have been instrumental in this turn-around.

The report of the OIG gives a false sense of the condition of the inventory because it has no baseline from which to compare. It simply chose 26 properties from an inventory of 3,500 (representing less than 1% of GFR's inventory) and concluded from this non-representative sample that "GFR did not preserve, protect and maintain HUD owned properties." This conclusion is overreaching given the data sampled and fails to compare the condition of the inventory today against what it was when GFR took over ten months earlier. GFR has not yet completed its first year with an inventory that was riddled with deferred maintenance but the opinions of the communities that GFR serves are contrary to the inferences in the OIG Report.

GFR inspectors are graded monthly based on the quality of their work.

Every month, GFR's inspectors in this region (numbering as many as 50) perform over 8,000 inspections. These inspections are thorough and require the inspector to sign in at the property and complete a written form covering most major internal and external conditions at the property. Given this number of inspections, and given the intensity involved in starting up this contract in its first year, there will undoubtedly be a greater number of deficiencies at this stage of the contract. As the OIG Report notes, however, GFR has taken a number of steps to reduce the deficiencies as it progresses under this Contract. In June, 2000, GFR implemented a comprehensive inspector grading program which requires quality control inspectors to follow behind routine inspectors to review their work and to assign a percentage grade based on performance. These grades are reviewed monthly by management and training is provided to inspectors who do not perform to expectations. Inspectors who fail to improve over several months will be subject to additional corrective measures. The early results of this program have been extremely promising and, as GFR moves into its second year (which is, in reality the first "normal" year under this Contract), we are confident that this program will make GFR's inspectors even better.

The OIG Report is critical of GFR's inspection quality control prior to June, 2000, not because the program was ineffective, but solely because GFR did not produce documents to support it. The "documents" that the OIG seeks, to verify the effectiveness of GFR's prior re-inspection program, are actually the inspection reports themselves. They are available in the files that the OIG has had access to for four months⁴. To ask GFR to spend numerous hours segregating these documents from the files is neither reasonable nor a requirement of the Contract. The fact that GFR did not produce these documents does not mean they do not exist nor does it mean the program was ineffective. To the contrary, they exist and have been available to the OIG during its entire audit.

GFR strongly disagrees with the finding that "management controls over correcting reported deficiencies were weak."

GFR strongly disagrees with the finding that "management controls over correcting reported deficiencies were weak." GFR's internal system, REAM, carefully tracks work order assignments and reports are run daily and weekly for management to track status and trends. Examples of many of these reports were provided to the OIG. The example of a control cited by the OIG Report is only one of many and the report's inference that it is the only such control is misleading and presents an inaccurate representation of GFR's systems and procedures.

The OIG's statement in the introductory paragraph of this finding (attributed to GFR's Assistant Vice President) is false and GFR denies not only the veracity of the statement but also that this statement was ever made. It should be noted that the author of the OIG Report did not hear this statement. The Report is including this statement based on the hearsay of an assistant to a field auditor. This assistant, however, on several occasions during the audit, proved incapable of understanding information provided to him by a number of GFR officials. His notes were notoriously unreliable as evidenced by the numerous times GFR officials would correct his notes from previous conversations. On some occasions, GFR's Contract Manager would spend hours explaining the Contract to this assistant and reviewing case files only to find some days later that he was still working under the same erroneous

⁴ The OIG began its audit of GFR's Chicago office in the last week of April, 2000. A staff of three full time and one part time auditors spent most of four months reviewing GFR's Chicago operation in intense detail.

understanding of HUD procedures. Whether the assistant took something GFR's Asst. VP said out of context, or simply made an error in his notes, is immaterial. What's important is that such a provocative statement should not have been included in the report without verification of its veracity.

The OIG's statement in the introductory paragraph of this finding (attributed to GFR's Assistant Vice President) is false and GFR denies not only the veracity of the statement but also that this statement was ever made.

In addition to the unreliability of its source, this statement is not credible on its face, yet, for some inexplicable reason, the author of the OIG Report elected not to obtain independent verification whether the statement was actually made or whether it was, in fact, true. Had the author of the OIG Report attempted to obtain either such verification before including such an inflammatory statement in his report, he would have learned that the statement was never made and that its contents were patently untrue. If it were true, then the sign-in sheets inside HUD Homes would not have GFR Inspection sign-ins which correspond with the written inspection reports. The truth is that the sign-in sheets and the inspection reports *do* correspond thereby evidencing that, in fact, the statement attributed to the Asst. VP was untrue.

Should the OIG be required to verify every single statement made by a GFR employee during the course of an audit? No. In this instance, however, knowing the enormously incendiary nature of the statement, and knowing that the OIG had no independent verification of its veracity, the OIG should have contacted GFR's senior management for verification before including it in its report. This is not a matter of courtesy, it is a matter of being thorough and making sure that individuals and companies are not defamed in a public report.

One is left to ask why the statement was included at all, unless it was intended to unfairly prejudice GFR. The inciting statement is made yet the OIG offers no documentary or evidentiary support. If it were true, the OIG, who had a team of four auditors spending full time for four months in GFR's offices, would have provided support.

There is no support because the statement was not made.

There is no support because the statement is untrue.

GFR continues to work to improve its procedures in the field and in the office to see that deficient property conditions are identified and, when required under the Contract, are timely remedied. With the implementation of its own inspector grading program (prior to the release of these findings), GFR had already addressed the recommendations of the OIG in this finding. The improvement of the inventory to date has been measurable and GFR's expects to see this trend continue as it evolves from cleaning up years of neglect to maintaining a fresh inventory.

FHA ROSTER APPRAISERS

Auditee Comments

Exhibit “1” of HUD’s Management and Marketing Contract (the “Contract”) sets forth the requirements for the appraisal process. Unfortunately, the appraiser requirements in this Exhibit are ambiguous and do not directly cover the common situation where licensed appraisers perform fieldwork under the supervision of an appraiser on the HUD Lender Selection Roster (the “Roster”). A review of the Contract language clearly demonstrates the ambiguity in this issue.

The M&M Contract contains conflicting requirements concerning appraiser requirements.

Before explaining the contractual ambiguities, GFR wishes to clarify a statement in the OIG’s introduction to this finding. The OIG states that GFR elected to require all appraisers to be on the Roster after “researching HUD policies.” This statement is not complete. In fact, as discussed in detail below, GFR does not concede the OIG’s premise that the M&M Contract requires the exclusive use of Roster appraisers. GFR contends that this issue is not clearly answered by either the Contract or the HUD Handbook. GFR elected to use Roster appraisers in an attempt to eliminate any potential problems that a buyer might encounter attributable to the ambiguity of this issue. (and out of respect for the Atlanta HOC’s directive on the issue)

Exhibit 1-1 of the Contract states that “appraisers must be on the HUD Lender Selection Roster, which is maintained by the Homeownership Centers.” The Contract also requires GFR to use appraisers who are “either state licensed or certified in the State where the property is located.” Finally, the Contract requires GFR to “ensure that each appraiser complies with the requirements of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA).” Unfortunately, these directives, though perhaps unintended, create a web of conflicting requirements that result in confusion relating to the use of licensed appraisers to assist in the preparation of appraisals⁵.

⁵ It should be noted that the OIG Report refers to HUD Handbook 4150.2 as providing additional appraiser requirements. The Contract, however, does not expressly include this reference. The Contract does make a later reference to the *appraisal* requirements in HUD Handbook 4150.1, but this handbook section does not include *appraiser* qualification standards. Nevertheless, even if 4150.2 is applicable, it does not add any requirement not already contained in the Contract.

The OIG Report does not distinguish between the two most common scenarios. In the first scenario, one appraiser performs all of the field and desk work and signs the appraisal. Under this situation, it is clear that the appraiser must be on the Roster. In the second scenario, which is far more common, a licensed and certified appraiser (who is not on the Roster) will assist a Roster appraiser in preparing the appraisal. The “assistant” signs the appraisal and the Roster appraiser reviews, approves and also signs the appraisal. This scenario is most common in larger appraisal companies where the corporation itself (or one representative) is on the Roster but each individual employee, while certified, is not on the Roster.

The M&M Contract is ambiguous on the issue of using non-Roster appraisers to assist in the preparation of appraisals.

It is this second scenario that the OIG Report finds unacceptable. GFR does not agree, however, with the OIG that this matter is clearly defined in the Contract. As discussed above, the Contract does not distinguish between assistant and supervisory appraiser. The Contract is ambiguous on this point and does not prohibit the use of licensed or certified appraisers who are under the supervision of Roster appraisers. The Contract is clear, however, on the requirement that GFR and its appraisers work within the parameters of FIRREA. Unlike the Contract, which is ambiguous on the issue of using supervisory appraisers, FIRREA has clear language on the topic. Section 1122(d) of FIRREA [which is codified at 12 U.S.C. § 3351(e)] provides that:

FIRREA expressly allows the use of supervisory appraisers provided that the “final appraisal document is approved and signed by an individual who is certified or licensed.”

A corporation, partnership or other business entity may provide appraisal services in connection with federally related transactions if such appraisal is prepared by individuals certified or licensed in accordance with the requirements of this title. An individual who is not a State certified or licensed appraiser may assist in the preparation of an appraisal if the assistant is under the direct supervision of a licensed or certified appraiser the final appraisal document is approved and signed by an individual who is certified or licensed.

Accordingly, while the Contract is silent on the use of appraisal assistants and supervisory appraisers, FIRREA speaks to the issue directly and allows for such arrangements provided that the “final appraisal document is approved and signed by an individual who is certified or licensed.”

GFR’s controls assured compliance with FIRREA as required by the Contract.

It is a long standing rule of contract construction in American jurisprudence that where general and specific provisions of a contract relate to the same matter, the more specific provision will control. 3 A. Corbin, *Corbin on Contracts* § 547, at 176 (1960). In the M&M Contract, the language contains: (1) the general language regarding the use of Roster appraisers (without any specific reference or prohibition concerning the use of assistants); and (2) the specific language imposing the obligations of FIRREA on GFR and its appraisers. In this instance, the specific language of the FIRREA provision would control over the other general language.

Clearly, based on the foregoing, there is some inherent ambiguity in the Contract as it relates to this Finding. GFR was operating under the provisions of FIRREA, which permits assistants to participate in the preparation of the appraisal under proper supervision. In these cases, GFR’s policy required that the supervisory appraiser be on the Roster and that he or she sign the appraisal in the space provided on the Uniform Residential Appraisal Report. These controls assured compliance with FIRREA and were not contrary to any express language in the Contract. Furthermore, these appraisals apparently met the requirements of the Direct Endorsement Underwriters as not one appraisal was returned to GFR as being insufficient or incomplete.

Evidently, in the summer of 2000, it became clear to HUD that this issue was indeed unclear. Apparently, the practice of using non-Roster appraisal assistants was commonplace nationwide. As a result, HUD has instructed all M&M Contractors to assure that all signatory appraisers are on the Roster and GFR has fully complied with this directive. Presumably, this directive will be followed with a contract

modification that will eliminate the ambiguity of this requirement.

TIMELINESS OF APPRAISALS AND DISPOSITION PROGRAMS

Auditee Comments

GFR has reduced average time on market for a HUD Home by 117 days in less than one year. This is a 48% reduction in time on market.

In evaluating the success of an M&M Contractor's property disposition process, one must look across its entire inventory and examine the timeliness and success of its sales programs. Selecting a small percentage of properties from a sales program that has processed over 10,000 houses does not allow this audit to reflect the real successes seen in the Midwest during GFR's transition year.

Since assuming responsibility for the Midwest, GFR has substantially increased the number of homes sold monthly while reducing the average time on market. These complementary results have produced unprecedented increase in the return to the FHA mortgage insurance fund. These tangible benefits result from GFR's efficiencies and the company's attention and typical adherence to the timelines set forth in the M&M Contract (the "Contract"). To achieve these fiscal improvements during a transitional year under the Contract, GFR and its staff focused on reducing average time on market for a HUD Home together with increasing the net return on each sale. When both of these objectives are met, the results are palpable.

For the twelve month period immediately preceding GFR's management of the HUD-owned inventory in the Midwest, a HUD Home averaged 243 days in inventory. Since GFR assumed responsibility in the Midwest, this time frame has declined dramatically to 126 days⁶. In eleven months, starting with a transitional inventory riddled with problems, GFR reduced the average time on market by 48%. It is well known that added time in inventory can increase property holding costs and exposure to deterioration or damage due to vandalism. With the average home in inventory 117 fewer days under GFR's management, HUD Homes have had less time to

⁶ This figure is based on the average days on market for each HUD Home that (1) GFR received into its inventory after Sept. 27, 1999 and (2) GFR sold and closed before August 24, 2000.

suffer from deferred maintenance or vandalism directly resulting in holding cost savings to HUD. Fewer days in inventory, coupled with better property conditions, have also resulted in increased return to HUD on the sale of the inventory.

In its first year, GFR has also produced a dramatic reduction in HUD's Turnover Rate⁷ in the A1 Contract area. According to HUD's SAMS System, in May 1999 (shortly following the inception of the M&M Program), the Turnover Rate for the A1 Contract area was an unprecedented 333.22 months. When GFR took over the area in September 1999, the Turnover Rate had dropped to 50.71 months. Since then, under GFR's management, the rate has plummeted. As of July 2000, GFR has reduced the Turnover Rate to 5.12 months. The importance of these figures cannot be overstated. GFR has taken an inventory that was virtually stagnant and has successfully implemented programs to move the inventory from acquisition to closing at a pace heretofore unseen in this area.

GFR's internal controls identify disposition delays and allow GFR to take appropriate remedial measures.

The OIG's review of a small sample of the homes sold in the last year overlooks this broader perspective and does not provide an appropriate overview of the program's success to date. As discussed below, while the sales process will inevitably suffer occasional delays, GFR's commitment to reducing the inventory has minimized these delays and has resulted in unmatched success in hastening the sale of HUD Homes.

Unfortunately, the OIG Report is devoid of any specific or identifiable case data, making it impossible to comment discretely on the origin of the individual findings. Additionally, these findings do not appear to account for the external forces affecting the practical application of the M&M Contract. The process of managing and marketing HUD-owned properties does not exist in a vacuum and is impacted

⁷ The "Turnover Rate" is a SAMS calculation that determines the number of months required to turn over a contractor's entire inventory assuming no further acquisitions. Accordingly, a smaller number indicates that the contractor is selling more homes (and selling them sooner) than a contractor with a higher Turnover Rate.

by a variety of uncontrollable variables and situations, many of which will be identified in this response.

GFR's internal controls focus intensely on timeframe performance. GFR provided the OIG with multiple examples of its Weekly Matrix Report, which is distributed to management throughout the company. This report identifies trends that show, for example, the timeliness of initial inspections and appraisals. In addition, individual department managers run daily reports from within GFR's REAM system to assure that properties are moving through the disposition process as quickly as possible. As shown below, the existence of delays is primarily a result of external factors. GFR's internal controls identify these delays and enable GFR's staff to take appropriate remedial action to redress delays as they are encountered.

TIMELY RECEIPT OF APPRAISALS

The finding that "GFR did not always appraise properties timely" is equally troublesome in light of the contributing causes, which may delay the anticipated delivery of appraisals. As with initial inspections, there are a multitude of factors that may surface, including the following, which lead to unfavorable timing in this category.

External factors, beyond GFR's control, can cause appraisal delays

The OIG Report contends that appraisals should be completed within ten business days "after HUD obtains title to the property." This approach, however, ignores the realities of property conveyance under the M&M program. GFR usually has no means of knowing when a property will come into its inventory other than the receipt of the electronic conveyance. Accordingly, until GFR receives the conveyance and enters it into the system, it cannot order its appraisal. It should also be noted that the Contract itself does not call for appraisals to be completed within ten days of HUD's acquisition of the property. To the contrary, the Contract requires that appraisals be obtained within ten business days of

“assignment” of the property (M&M Contract, Section C-2, IV)⁸.

- Much like the circumstances hampering the timely inspection of properties, appraisers are also challenged by incorrect or incomplete addresses. GFR attempts to issue appraisal instructions only after the correct information is obtained. ***Unless the property can be properly identified, appraisals cannot be completed in 10 days.***
- As discussed in the context of initial inspections, gaining access to condos in gated communities also creates delays. ***Unless access can be legally obtained, appraisals cannot be completed in 10 days.***
- Questionable title to properties deems premature appraisal attempts ill advised. ***Unless ownership can be confirmed, appraisals cannot be completed in 10 days.***
- If a site is discovered zoned commercial, a whole new set of instructions, licenses, criteria, and forms are required. Due to the specialty nature of this change and the appraisal itself, it takes more than the customary 10 days. ***The added factor of an atypical zoning prevents appraisals from being completed in 10 days.***
- If adverse inhabitants occupy a property, the appraiser is unable to enter. Appraisers have been denied access to properties by unexpected residents varying from dangerous animals to gang members. In these cases, legal action is often required which necessarily delays the appraisal. ***The presence of adverse occupants prevents appraisals from being completed in 10 days.***
- Health issues also surface causing delays in the completion of appraisals.

⁸ It should be noted that there is an internal contradiction within the M&M Contract that makes the commencement date for the appraisal timeframe unclear. See M&M Contract, Section C-2, V, Para. 9. Since it would be impossible to achieve contract compliance with the ten-day period commencing with HUD acquisition, GFR bases its timeframe calculation on the assignment date as provided by the Contract.

Methamphetamine labs, excessive blood, or drug paraphernalia, for example, require specialized removal and delay property inspection by the appraiser. ***The presence of unexpected materials prevents appraisals from being completed in 10 days.***

- In areas of rampant vandalism, locks may be tampered with denying the appraiser access between the time of the initial inspection and the next day when he arrives. ***Unexpected denial of access prevents appraisals from being completed in 10 days.***
- Deceptive tampering with addresses and/or unit numbers also interferes with the appraiser’s ability to obtain access to the correct unit. ***In cases of altered street or unit numbers, appraisals cannot be completed in 10 days.***
- There are also miscellaneous circumstances such as missing stairways, encroachments requiring surveys, or properties appearing to have two houses on one lot or two lots with one house in the middle. In these cases, further research is required to assure that the appraiser is analyzing the correct property and is able to inspect the entire building. ***In cases requiring additional research, appraisals cannot be completed in 10 days.***

TIMELY APPROVAL OF DISPOSITION PROGRAMS

The OIG Report contends that GFR “did not always approve property disposition programs timely”. This finding fails to consider the environment in which the sales disposition program operates and the external variables that interfere with the smooth transition from appraisal to listing.

Certain provisions of HUD’s Property Disposition Handbook are not feasible under the M&M Program.

The OIG Report, relying by reference on the HUD Property Disposition Handbook 4310.5, Rev 2, is critical of GFR’s property disposition program in those cases where a disposition has not been approved

within three days of receipt of appraisal. This criticism, however, is based on requirements that significantly predate the existence of the M&M program and once again ignores the presence of external factors.

The most recent draft of the Property Disposition Handbook is dated May 1994 and was written at a time when all HUD property disposition functions were handled in-house. A number of the guidelines in the Disposition Handbook are simply no longer feasible or workable under the M&M program. For example, the Property Disposition Handbook does not even allow for, or provide guidelines for, an electronic bidding system, which, under the M&M Contract, is the sole means of property disposition. With regard to three-day approvals of all dispositions, the Handbook directive was not drafted in light of the current system of electronic bidding.

To highlight the dated and inapposite approach of the Handbook, one need only review Section IV, paragraph 6-17 which governs disposition program processing (this is the same provision which contains the “three day” time frame which is the premise of this finding in the OIG Report). This Handbook section defines the “approval process” as the completion of the SAMS ACMC3 screen. The Handbook erroneously states, however, that the “recording of approval of the Disposition Program moves the case to Step 3.” In fact, under the current processing system, the approval of the disposition program moves the case to *Step 5*. In addition, recent changes in the SAMS program automatically converts properties to a Step 6 on the listing date (instead of on the approval date).

Blind adherence to the HUD Handbook by an M&M Contractor could create serious problems

While the Handbook is a helpful reference, blind adherence to its procedures by an M&M Contractor could create serious problems. For example, to sporadically approve disposition programs that cannot be moved to a Step 6 risks listing properties that may otherwise be cancelled for any of the following reasons. Title issues discovered at the last minute. Quality Control of physical condition of property discovers an unsafe condition.

- Discovery of adverse occupants

- Removal of the property from the market to accommodate the OIG Safe Home Program
- Dramatic change in condition due to extraordinary vandalism requiring reevaluation of the price or status
- Fire
- Demolition due to outstanding code violations pre-dating GFR
- Notification from mortgagees that the conveyance was improperly done and must be re-conveyed

Remedying these items would be made far more complicated if GFR were approving dispositions before the property was actually ready to list. Additionally, since timelines are the focus of this and many other monitoring efforts, early approval of dispositions would stretch the time in Step 6 (Step 5 for approved non-profit sales) causing more exceptions on the SAMS “Cases Exceeding Time in Current Step Report”. Early disposition approvals could also cause early re-analyzation of listings and a premature reduction in price, which ultimately can reduce the return to the FHA fund.

Unfortunately, the OIG Report does not provide specific examples of these delays. Many of these cases reviewed were properties received from the prior contractor in the transition and listed during the start-up phase of the contract. GFR officials discussed these examples with the auditor and, in each case, the vagaries of the transition (e.g., receiving more than 5,000 files in one day) were responsible for short delays.

CONCLUSION

GFR’s success in reducing inventory by 40% is indicative of its overall conformity to the intended timeframes.

During GFR’s first year in the Midwest, approximately 7,500 appraisals were ordered, the majority of which were delivered within the allotted time. Over 10,000 new acquisitions were processed and inspected, most without incident or delay. Approximately 15,000 properties have been listed for sale, having completed the appropriate preparations

and data entry. Inventory reduction has been unprecedented, dropping a swollen inventory of nearly 5,800 homes to a more manageable level under 3,500 in less than one year.

These statistics fully supports GFR's claim of success and overall conformity to the intended timeframes. If GFR had failed to comply with the timeframes in any material way, the results would surely have manifested themselves in numbers contrary to those herein presented. GFR is committed to meeting contractual timeframes wherever possible and strives to dispose of the HUD inventory in a rapid, but controlled manner.

Distribution

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