AUDIT REPORT

AUDIT OF THE SUPPORTIVE HOUSING PROGRAM
GRANT TO THE
NATIONAL SCHOLARSHIP SERVICE AND
VETERAN'S OPPORTUNITY AND RESOURCE CENTER
ATLANTA, GEORGIA

2002-AT-1003

JULY 25, 2002

OFFICE OF AUDIT, REGION 4

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audit report

Issue Date July 25, 2002	
Audit Case Number 2002-AT-1003	

TO: John Perry, Director, Office of Community Planning and Development, 4AD

N. H. Cooper

FROM: Nancy H. Cooper
Regional Inspector General for Audit, 4AGA

SUBJECT: Audit of SHP Grant to the National Scholarship Service and
Veteran's Opportunity and Resource Center, Inc.
Atlanta, Georgia

At your request, we completed an audit of the Supportive Housing Program (SHP) grant and matching fund expenditures by the National Scholarship Service (NSS)/Veteran's Opportunity and Resource Center, Inc. (VORCI). We initiated the audit based on your concerns that NSS-VORCI could not adequately account for its 1997 SHP grant expenditures and could not identify eligible matching fund expenditures. You also expressed concerns about VORCI properly accounting for grant and matching fund expenditures from a 2000 renewal grant.

In accordance with the Department of Housing and Urban Development (HUD) Handbook 2000.06 REV-3, within 60 days please provide us, for each recommendation without management decisions, 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. Additional status reports are required at 90 days and 120 days after report issuance for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the audit.

We provided a copy of this memorandum to NSS and VORCI.

If you have any questions, please contact me or contact Terry Cover, Assistant Regional Inspector General for Audit, at (404) 331-3369.

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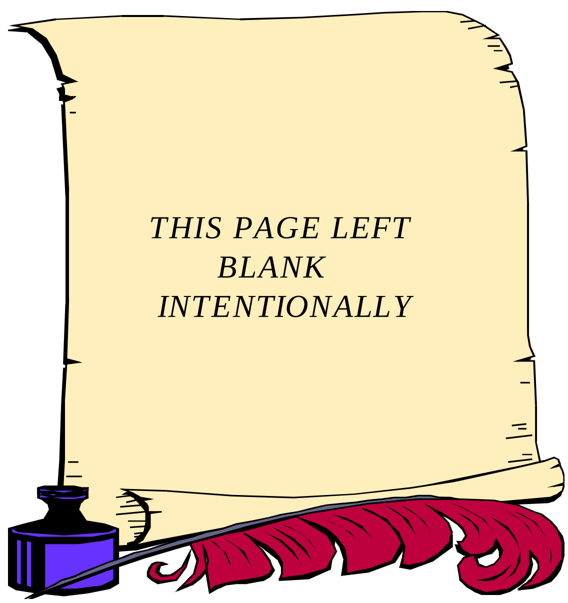
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Executive Summary

We audited NSS-VORCI's expenditures of a 3-year 1997 Supportive Housing Grant for $1,885,338 as requested by the Director, Office of Community Planning and Development, in Atlanta, Georgia. Our objectives were to determine whether grant and matching funds were properly accounted for and expended for eligible costs. We also assessed whether a subsequent 2000 renewal grant was properly accounted for.

NSS-VORCI's management did not responsibly manage grant accounting, expenditures, and compliance with SHP requirements. They did not establish (1) accounting system procedures and controls needed to comply with Federal requirements for grant fund accounting, (2) procedures to ensure only eligible and necessary expenditures were charged to SHP grant funds, and (3) procedures to monitor and compare SHP expenditures to the approved budget. Salaries and other costs that benefited multiple programs were not allocated to programs and fund sources in a documented and systematic manner. VORCI's accounting journals and general ledger were incomplete, inaccurate, and contained numerous misclassified costs. As a result, VORCI spent grant funds on ineligible and unnecessary costs, deviated significantly from its approved budget without HUD approval, and did not meet matching fund requirements. We attribute these conditions to NSS-VORCI's Executive Director and Board of Directors not ensuring responsible management practices and compliance with HUD requirements for grants management.

NSS-VORCI expended about 25 percent of 1997 SHP grant funds for ineligible and unsupported costs. Costs incurred were frequently not in the approved budget, were for unapproved housing facilities, or were not in compliance with SHP program regulations. The improper expenditures occurred because NSS-VORCI management did not establish management controls and did not monitor expenses to ensure that grant funds were spent for eligible purposes and were adequately documented. As a result, grant fund expenditures included $158,330 of ineligible costs and $313,811 of unsupported costs. Additionally, $34,443 of operating expenditures was ineligible for HUD funding because it was not matched by VORCI.

Recommendations

We recommend that you terminate further SHP grant funding to VORCI. New funding should not be considered until VORCI's Board of Directors and Executive Director have established written management and accounting procedures and controls to ensure accounting is complete and accurate, and expenditures are monitored for eligibility, proper support, and correlation to the budget. We recommend that you require VORCI to replace its Executive Director and strengthen Board oversight processes before providing any new grant funding. We also recommend you require VORCI to repay $158,330 for ineligible costs, and $34,443 for grant funds that were not matched. VORCI should also provide adequate support for $313,811 of unsupported costs or repay those funds to HUD.


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Abbreviations

CFR	Code of Federal Regulations
HUD	Department of Housing and Urban Development
NSS	National Scholarship Service
OIG	Office of Inspector General
SHP	Supportive Housing Program
VORCI	Veteran’s Opportunity and Resource Center, Inc.

Introduction

Title IV of the Stewart B. McKinney Homeless Assistance Act authorized the SHP. The program is designed to promote the development of supportive housing and services. The program encourages the use of innovative approaches to assist homeless persons and provides supportive housing to enable them to live as independently as possible. Grant funds may be used to (1) establish new supportive housing facilities or new facilities to provide supportive services; (2) expand existing facilities in order to increase the number of homeless persons served; (3) bring existing facilities up to a level that meets health and safety standards; (4) provide additional supportive services for residents of supportive housing or for homeless persons not residing in supportive housing; (5) purchase HUD-owned single family properties for use as a homeless facility; and (6) continue funding supportive housing where the recipient has received funding for leasing, supportive services, or operating costs. In its technical submission to HUD, NSS (formerly the National Scholarship Service and Fund for Negro Students) proposed to provide new and expanded transitional housing with supportive services for the homeless veteran population of Atlanta. It stated that the expansion project would increase the number of homeless persons served and provide additional supportive services for residents of supportive housing and/or homeless persons not residing in supportive housing.

The NSS is a nonprofit community based organization and has provided services in Atlanta since 1947. NSS veterans programs began in 1972 and included two components that provided a continuum of care for homeless veterans: Harris House Veterans Center, providing transitional housing and supportive services since 1988; and Veterans Upward Bound, providing educational enhancement since 1972. VORCI was a subsidiary of NSS, but separated from NSS effective October 2, 2000. A 13-member board administers the VORCI organization. NSS and VORCI offices are located at 2001 Martin Luther King Jr., Drive, Atlanta, Georgia.

On August 4, 1997, HUD awarded NSS $1,885,338 in SHP funds for a 3-year grant period to provide new and expanded transitional housing and additional supportive services for residents of supportive housing and/or homeless persons not residing in supportive housing. The grant period was from March 1, 1998, through February 28, 2001. On October 2, 2000, the grant agreement was amended to change the grantee to VORCI, which then became responsible for grant administration. At that time, VORCI obtained the SHP accounting records that had been maintained by NSS and reconstructed them. Grant funding initially included $891,720 for supportive services, $503,840 for operations, $400,000 for rehabilitation of two scattered site apartment complexes, which consisted of 48 units, and $89,778 for administration. In February 2000, at the grantee's request, HUD redistributed $5,985 between budget line items. Consequently, funding levels changed to $888,258 for supportive services, $509,825 for operations, $400,000 for rehabilitation and $87,255 for administration.

On March 1, 2001, HUD awarded VORCI a $440,319 SHP renewal grant for a 1-year period. Grant funding included supportive services ($241,282), operations ($178,069), and administration ($20,968).

Audit Objectives

Our audit objectives were to determine whether 1) expenditures of 1997 SHP grant funds and required matching funds were adequately accounted for and eligible as specified by SHP program regulations, and 2) VORCI's current accounting for the 2000 renewal grant and matching funds complied with Federal requirements.

Audit Scope and Methodology

To accomplish our objectives, we reviewed HUD records and NSS/VORCI accounting records and funding agreements at their offices in Atlanta, Georgia, interviewed VORCI staff and visited SHP housing project sites at 2099 Martin Luther King Jr. Drive and 156 Fairfield Place in Atlanta. Since NSS-VORCI could not provide adequate accounting records and could not identify matching fund expenditures, we expanded our audit testing. We reviewed all expenditures ($2,847,719) charged to VORCI's Harris House Veteran's Center accounts to identify eligible SHP costs including matching costs, and we traced those costs to supporting documents and bank statements to confirm payment and amount. We obtained and analyzed payroll records for the grant period from a payroll processing company employed by NSS-VORCI, and estimated eligible salary costs. Lastly, we assessed the adequacy of accounting records for the 2000 renewal grant by reviewing available reports from VORCI's new accounting system and discussion with a VORCI official.

Our audit of the 1997 SHP grant covered the period March 1, 1998, through February 28, 2001. We assessed current accounting reports for the renewal grant as of September 21, 2001. We performed the audit from August 2001 through April 2002. We conducted the audit in accordance with generally accepted government auditing standards.

We provided a copy of this report to the Assistant Secretary for Community Planning and Development and to NSS/VORCI.

Management Did Not Responsibly Manage Grant Funds, Accounting, and Compliance With SHP Requirements

NSS-VORCI's management did not responsibly manage grant accounting, expenditures, and compliance with SHP requirements. They did not establish (1) accounting system procedures and controls needed to comply with Federal requirements for grant fund accounting, (2) procedures to ensure only eligible and necessary expenditures were charged to SHP grant funds, and (3) procedures to monitor and compare SHP expenditures to the approved budget. Salaries and other costs that benefited multiple programs were not allocated to programs and fund sources in a documented and systematic manner. VORCI's accounting journals and general ledger were incomplete, inaccurate, and contained numerous misclassified costs. As a result, VORCI spent grant funds on ineligible and unnecessary costs (see Finding 2), deviated significantly from its approved budget without HUD approval, and did not meet matching fund requirements. We attribute these conditions to NSS-VORCI's Executive Director and Board of Directors not ensuring responsible management practices and compliance with HUD requirements for grants management. As a result, VORCI could not (1) reliably account for its expenditures of 1997 and 2000 SHP grant and matching funds, (2) identify eligible expenditures by approved grant and funding purpose (operating, supportive services, and administration), (3) identify employee salaries charged to grant funds, and (4) monitor and compare SHP expenditures to the approved budget.

Title 24 of the Code of Federal Regulations (CFR), Part 84.21(b)(1), (2) and (4), require the grant recipient to maintain a financial management system that provides: (1) accurate, current and complete disclosure of the financial results of each federally-sponsored project, (2) records that adequately identify the source and application of funds for federally-sponsored activities, and (3) a comparison of outlays with budget amounts.

Office of Management and Budget Circular A-110, paragraphs 25 (b) and (c), state that recipients are required to report deviations from budget and program plans, and request prior approvals for budget and program plan revision. It states that recipients shall request prior approval from Federal awarding agencies for (1) a change in the scope of the project or program, (2) the need for additional federal funding, or (3) the transfer of amounts budgeted for indirect costs to absorb increases in direct costs, or vice versa, if approval is required by the Federal awarding agency.

Title 24 of CFR 583.405 (a)(1) states that a recipient may not make any significant changes to an approved program without prior HUD approval. A significant change is specified as a shift of more than 10 percent of funds from one approved activity to another.

Accounting for SHP Expenditures and Receipts Was Incomplete and Inaccurate

During the 3-year 1997 SHP grant period, NSS-VORCI expended $1,885,338 in grant funds without classifying any expenditures to the three grant categories of SHP operating, supportive services, and administration.

VORCI charged all of its expenditures (excluding SHP rehab costs) to two cost centers: Harris House, which included SHP activities, and Veterans Upward Bound. After the grant period ended, HUD officials requested accounting records for SHP expenditures, which VORCI could not provide. As a result, VORCI's Administrative Operations Manager reviewed and classified Harris House expenditures to the three grant-funding categories after the fact. She said that NSS' accounting system was incapable of tracking accounting entries in a manner that would satisfy grant accounting and reporting requirements, and she had reconstructed the SHP records using bank statements and disbursement request documents. Her review did not identify matching fund expenditures and classified only enough Harris House expenses to equal the SHP grant. Afterward, the general ledger identified costs VORCI charged to HUD funds, but did not show other charges pertinent to the SHP. Consequently, the general ledger could not be used to prepare a summation of SHP expenditures during the 1997 grant period.

VORCI maintained a general ledger and cash receipts and disbursements journals. We noted numerous inaccuracies in these accounting records for both the 1997 and 2000 SHP grants. NSS-VORCI charged numerous expenses to accounts that were not listed in its Chart of Accounts. VORCI's general ledger contained entries that had been rounded, while the disbursements journal entries were for actual amounts.

VORCI's cash receipts journal was inaccurate. VORCI had not accounted for all draw downs of grant funds. VORCI's accounting records did not show any receipts from HUD during the month of August 2000, while the HUD LOCCS report and bank statements indicated that on August 2, 2000, $13,995 was drawn down from operating funds, $24,770 from supportive services funds, and $2,493 from administrative funds. VORCI also recorded draws prior to

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actually making and receiving them. For example, VORCI recorded receipt of a HUD draw on April 1, 1999, when the LOCCS report showed a transaction date of April 12, 1999. This occurred again in May and December 1999. We also noted that VORCI had incorrectly recorded $37,346 in security deposits collected from SHP participants. VORCI recorded the security deposits as rent collections (revenue) and did not record the deposits as a liability.

As of September 21, 2001, VORCI had drawn $293,544, or 67 percent, of its 2000 renewal grant. Although we requested accounting records for the renewal grant several times, we were only provided a cash receipts journal. VORCI could not produce an accurate general ledger and disbursements journal for the renewal grant. VORCI's Administrative Operations Manager told us that she had charged SHP expenditures to other program accounts because VORCI was not allowed to draw renewal grant funds until June 2001. Subsequently, VORCI had not adjusted its accounting records to charge the expenses to SHP accounts. VORCI's current accounting system (hardware and software), if properly utilized, was capable of complete grant accounting.

Salary and Other Costs Benefiting Multiple Programs Were Not Properly Allocated

NSS-VORCI had not established a cost allocation plan. Direct and indirect costs that benefited multiple programs were not allocated to programs and fund sources in a supported and systematic manner. Salaries were VORCI's largest expense, but its records did not identify which employees were charged to the three SHP grant categories. VORCI's Executive Director, administrative staff and SHP operating staff should have been allocated between the SHP categories and non-SHP activities. No rational basis was used to allocate salaries to the grant categories. Salaries charged to the SHP operating category included portions of only two biweekly payrolls in March 1998 and one full biweekly payroll in November 1998. Salaries charged to the administration category included varying portions of 12 biweekly payrolls between May 1998 and April 2000. The majority of salaries were charged to the largest grant category, support services. We obtained detailed payroll information from a payroll processing company used by NSS-VORCI and used it to estimate eligible salary charges (see Finding 2). VORCI could have used the payroll company to allocate charges to multiple cost centers and provide payroll reports supporting salary costs charged to the SHP grant categories. Other general administration costs, such as audit costs, telephone costs, etc., should also have been allocated between programs and funding sources but were not.

Expenditures Significantly Deviated From The Approved SHP Budget

Because expenses were not classified during the grant period, VORCI management had no capability to measure expenditures against the approved SHP budget. The Executive Director did not adhere to the budget for the 1997 SHP grant and sought no prior approval from HUD for significant variances from the budget. VORCI charged general and indirect costs to SHP funds when (1) those costs were not included in their SHP budget, and (2) a portion of those costs must be allocated to other programs and fund sources.

In its SHP operating budget, VORCI identified operating costs for two building sites used as supportive housing (2099 MLK and 156 Fairfield). HUD requirements stipulate that operating costs are those costs associated with the day-to-day operations of the supportive housing. VORCI incurred operating costs for at least five other locations, one of which was their office location and one housing site that HUD approved for SHP use during the grant period. The other three housing facilities and the office were not approved for SHP funding by HUD. VORCI budgeted $351,360 for operating salaries and fringe benefits, but charged only $21,170. VORCI budgeted $9,000 of operating funds for telephones, but charged $94,991. VORCI also charged unbudgeted general office costs to the operating portion of the HUD grant. For example, VORCI charged $37,349 for office supplies, $24,414 for office equipment, and $29,555 for equipment maintenance. These costs are not associated with day-to-day operation of the supportive housing, and do not appear to be eligible under 24 CFR Part 583.125. However, HUD program officials stated that some general office expenses pertaining to operation of the supportive housing could be eligible (see Finding 2 for further discussion.)

In its supportive services budget, VORCI included $576,000 for salaries for six full time employees. However, VORCI charged salaries totaling $842,111 during the grant period. We noted that the number of supportive services employees paid each biweekly payroll period varied from 4 to 11 during the grant period. Salaries charged to HUD included a duplicate charge of $9,381. The salaries charged exceeded the budget by $266,111, or 14 percent of the total $1,885,338 grant and constituted a significant change without HUD approval. VORCI also budgeted $96,000 for drug testing of participants, but charged only $1,231 for drug testing supplies, of which, $557 had been incorrectly charged to the operating portion of the grant, and $674 had been incorrectly charged to administration. According to the Executive Director, the Veteran's Administration began to offer free drug testing and therefore, VORCI did not have to expend the total amount it had budgeted for this program activity.

The Executive Director acknowledged that budget revisions should have been made and submitted to HUD.

VORCI Could Not Identify Matching Fund Expenditures

For the 1997 SHP grant, NSS-VORCI was required to provide matching funds for the rehabilitation and operating fund portions of the grant. VORCI was required to match 100 percent of the rehabilitation grant funds, and provide 25 percent of operating funds expended during the first 2 grant years and 50 percent in the third year. VORCI's required matching contributions were $400,000 for rehabilitation and $244,000 for operating costs. We reviewed funding source records and determined that VORCI had received sufficient funds to meet the HUD matching requirements. However, VORCI's accounting records did not identify matching fund expenditures. The Executive Director maintained that VORCI had spent more than enough to meet matching requirements, and therefore he believed it was apparent the requirements were met without specifically identifying costs.

NSS-VORCI maintained a separate bank account for SHP rehabilitation activities. By reviewing records of disbursements from the separate bank account, we determined that the $400,000 rehab grant and matching funds exceeding $400,000 were expended for eligible purposes.

We could not identify enough eligible SHP operating costs to meet the required match of $244,000. We identified $962,381 in expenditures charged to Harris House that had

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not been charged to the SHP. Most of those expenditures were not eligible as SHP operating costs or did not have adequate supporting documentation to show the purpose of the expenditure. We identified $730,046 that was ineligible, including $299,428 in debt service payments, $64,089 for salaries, $52,413 for employee fringe benefits, $2,366 for operating non-SHP facilities, and $27,389 for credit card payments. The remaining $284,361 of ineligible costs was for various expenditures, such as rental of unapproved (non-SHP) facilities, legal fees, pre-development costs, travel expenses, subscriptions and membership dues. Program regulations prohibit the use of operating funds for these types of expenses and for debt payments. The salaries and fringe benefits were unsupported as to employee name and whether the SHP benefited and were deemed ineligible based on our estimates of eligible salaries (see Finding 2 for estimates of eligible salaries and fringe benefits).

We identified only $32,262 of eligible operating costs available to meet the $244,000 matching-fund requirement. We also identified $30,984 of potentially eligible operating type costs such as telephone charges, work performed by contract employees, utilities, property insurance, and grounds maintenance. However, the supporting documentation did not identify the facility locations for these costs. The remaining $169,090 consisted of payments for contract employees, administrative fees, and general office expenses, with documentation inadequate to show the purpose of the expense and/or whether it pertained to operation of SHP housing. As noted above, only the portion of administrative and general office expenses pertaining to approved supportive housing may be charged to operating grant funds. Thus, we concluded that VORCI did not incur sufficient eligible matching expenditures to justify receipt of the full SHP grant for operations (see also Finding 2.)

Transactions Indicating Abuse of Funds

VORCI paid $23,976 for questionable charges by its Executive Director to a credit card issued for travel purposes. VORCI also paid interest to a Board member equal to a 240 percent annual interest rate.

We reviewed available credit card statements for potentially eligible matching costs and found many questionable charges that did not appear to benefit VORCI or the SHP.

For example, credit card charges included: 16 transactions at the New South Package Store totaling $1,124; 25 payments to Regal Car Wash totaling $748; 68 gasoline purchases totaling $2,003; 7 transactions at a Ford dealer totaling $806; 11 transactions at Home Depot totaling $1,543; 1 transaction at Radio Active Car Stereos Inc. for $991; and numerous other transactions that appeared to be of a personal nature. VORCI did not have receipts to show what these purchases were for. All of the questionable credit card charges were made in the Atlanta metro area and nearly all were in the vicinity of the Executive Director's residence. The types of charges and the complete absence of receipts indicate abuse of funds by the Executive Director. Since VORCI commingled SHP funds with other funds, did not account for expenses by fund source, and cannot document eligible expenditures equal the SHP grant, misuse of SHP funds may have occurred.

NSS issued the credit card to VORCI's Executive Director and told us it should have been used for business travel purposes only. According to NSS officials, they did not require the Executive Director to sign the standard credit card agreement, which all NSS employees must sign, but he knew what the credit card restrictions were. NSS officials stated they reviewed the credit card statements, but never performed a thorough review. They further stated that they questioned some charges and were told by the Executive Director that they related to program activities. They did not question it any further, but acknowledged they should have looked closer at the charges.

VORCI obtained a short-term $30,000 loan, not to exceed 30 days, from a Board member. The Executive Director told us that the loan was needed to cover payroll in May 2001, and was authorized by the Board's executive committee. He said he recommended the 10 percent interest rate as being fair. However, $33,000 was repaid in 2 weeks, equaling an effective annual interest rate of 240 percent. VORCI could not provide a signed loan agreement. VORCI had not classified the source of funds used to pay this debt, but we determined from accounting and bank records that HUD funds were used to repay the loan.

Misclassified Costs

VORCI misclassified operating, supportive services and administrative costs totaling $35,425. The spreadsheet of SHP charges prepared by VORCI incorrectly listed $6,342 in supportive services and operating costs as administrative costs, $28,284 in supportive services costs as operating costs, and $798 in administrative costs as supportive services costs. (See Appendix D for audit adjustment of those costs.)

Auditee Comments

"VORCI did establish a system of allocating employee salaries among our various programs. Salaried employees are initially charged to the programs based on percentage of time spent, however, our system does not involve a periodic formal confirmation of the percentage of time spent on each activity. The accountant was charged with assuring that the allocations were consistent and properly charged to the SHP grant categories.

"We have used our external auditors to assist us with identifying the year-end adjusting journal entries, such as recording security deposit liabilities, accounts payable, cash receipts classifications, etc. The OIG auditors may not have taken these adjustments into account during their audit.

"Unfortunately, our accounting system did not specifically identify and classify the expenditures as "SHP matching expenditures," however our records do identify the expenditures and we can provide specific (and sufficient) expenditure details to justify the match.

"VORCI will revisit its general ledger chart-of-accounts to be sure sufficient accounts are established to permit classification of expenditures by SHP budget categories. Our revised system will include posting the HUD approved budget line items so that we can monitor budget compliance. The OIG has indicated that our Peachtree Accounting software is adequate provided that it is properly maintained. VORCI will also establish a cost allocation plan to ensure all direct costs are properly allocated and all indirect costs are allocated using an acceptable methodology. To solve the matching funds requirement, we will establish specific general ledger accounts for the

SHP grant entitled “SHP matching funds” in which we will post our various matching expenditures consistent with HUD regulations. This will provide an unquestionable audit trail of our matching funds.

“We will move expeditiously to hire a more experienced accountant with specific nonprofit grants accounting experience, preferably with five or more years of field experience.

“The Executive Committee will investigate the abuse of funds referenced in the OIG audit and issue written recommendations to the Board of Directors. The written report will be shared with OIG and HUD.

“As for future compliance, we will modify our corporate by-laws to establish a standing audit and finance committee to strengthen the Board of Directors’ oversight of fiscal management and audit resolution. In keeping with our existing five-year action plan, we have already increased the size of the Board of Directors and filled the vacant positions with persons with more fiscal experience.

“As evidence of our compliance, we have requested that our auditors (The Wesley Peachtree Group), who have significant nonprofit and governmental grants experience, provide a certification to HUD of our accounting system compliance within six (6) months.”

OIG Evaluation of Auditee Comments

As noted in Finding 1, salary charges posted in VORCI’s general ledger and to the spreadsheet (prepared after the fact to document charges to the SHP grant categories), were not allocated by any rational or documented methodology. VORCI’s bookkeeper was not an accountant and the Executive Director and Board provided no written policies and procedures to ensure grant accounting was properly performed.

Adjusting entries by VORCI’s independent auditor have no bearing on the spreadsheet of SHP charges prepared by VORCI. SHP expenditures were not identified in VORCI’s general ledger until after the 3-year grant period was over.

Prior to our audit, HUD program staff requested that VORCI's Executive Director identify matching expenditures. During the audit, OIG made the same request. The Executive Director ignored both requests, stating that expenditures not charged to SHP far exceeded the required match and thus the adequacy of matching costs was obvious. As noted in Finding 1, there were insufficient eligible costs charged to the Harris House cost center, and not charged to SHP funds, to satisfy the matching funds requirement.

As noted in our recommendations, VORCI should be required to demonstrate that it has established an adequate financial management and accounting system by producing actual monthly financial reports from its general ledger, before HUD considers providing any further grant funds. VORCI needs to develop written procedures specifying its accounting approval process, other accounting controls, a budget monitoring process, and delineating eligible costs for the SHP grant categories (versus other non-SHP activities) and methods for allocating salaries and other direct and indirect costs between SHP and other activities. As noted in the report section, Follow up on Prior Audits, VORCI's independent auditor did not identify any of the accounting and control deficiencies noted in this report, and we concluded that its audit opinions on VORCI's financial statements could not be relied upon.

Regarding proposed changes in Board composition and function, VORCI will need to provide evidence of actual changes, to demonstrate to HUD that Board oversight will be satisfactorily improved. We have added recommendation 1C to separate recommended actions relating to the Executive Director and the Board, which were previously both included in 1B.

Recommendations

We recommend that HUD:

1A. Terminate further SHP grant funding to VORCI. VORCI should not be considered for new funding until its Board of Directors and Executive Director have established written procedures and controls to ensure accounting is complete and accurate, and

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expenditures are monitored for eligibility, need, and correlation to the budget. VORCI should also demonstrate complete and accurate accounting for its activities before new grants are considered.

1B. Require that VORCI strengthen Board oversight processes before providing any further grant funding.

1C. Require VORCI to replace its Executive Director before providing any further grant funds and consider a Limited Denial of Participation of the Executive Director.


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NSS-VORCI Expended SHP Funds For Ineligible and Unsupported Costs

NSS-VORCI expended about 25 percent of 1997 SHP grant funds for ineligible and unsupported costs. Costs incurred were frequently not in the approved budget, were for unapproved housing facilities, or were not in compliance with SHP program regulations. The improper expenditures occurred because NSS-VORCI management did not establish management controls (see Finding 1) and did not monitor expenses to ensure that grant funds were spent for eligible purposes and were adequately documented. As a result, grant fund expenditures included $158,330 of ineligible costs and $313,811 of unsupported costs. Additionally, $34,443 of operating expenditures was ineligible for HUD funding because it was not matched by VORCI. See Appendix A for a summary of questioned costs.

Title 24 CFR 84.21(b)(3) and (7) require that a recipient's financial management system provide: (1) effective control over and accountability for all funds, property and assets, (2) adequate safeguards for all such assets and assurance that they are used solely for authorized purposes, and (3) accounting records that are supported by source documentation.

NSS was the original applicant for the SHP grant. Its Executive Director said that housing for the homeless was a VORCI initiative, and NSS gave VORCI's Executive Director full authority and responsibility for administering the SHP grant. VORCI was responsible for the allocation of expenses to SHP funds and performed this classification after the grant period and after the funds had been spent.

Ineligible Costs

NSS-VORCI charged $158,330 in ineligible costs to the 1997 HUD SHP grant. Of this amount, $135,141 was charged to operating, $12,393 to supportive services, and $10,796 to administration funds. See Appendix B for a detailed listing of ineligible costs.

- VORCI charged $23,075 for telephone costs that did not benefit the SHP, including payments for financing the telephone system, ISDN lines, and internet services. Financing costs are not eligible. The ISDN and internet costs primarily served a computer lab used in a non-SHP program. VORCI also charged various other ineligible costs including $18,249 for legal fees, $2,104 for office supplies, $3,621 for utilities, $239 for postage, $9,008 for equipment, $11,009 for facility maintenance, $249 for security equipment, $318 for insurance, $672 for membership dues, $40 for subscriptions, and $1,332 for property taxes. These costs were ineligible under SHP regulations and/or were related to non-SHP facilities and activities.

During the audit exit discussion, HUD officials stated that operating grant funds could be used for some general office or administrative expenses, if supported as pertaining to the day-to-day operation of supportive housing as prescribed in Title 24 CFR Part 583.125. No general office costs were included in the SHP operating budget. However, based on HUD's interpretation, we reclassified $113,570 from ineligible costs to unsupported costs in this final audit report. These costs are unsupported because VORCI did not maintain documentation to identify costs pertaining to the SHP versus other programs and activities, and/or did not maintain invoices to document the nature of the expenses.

- VORCI duplicated $6,677 of operating charges for various transactions including office supplies, maintenance, and repairs.

- VORCI expended $46,920 for operation of existing, non-approved housing and office facilities. In its technical submission to HUD, VORCI identified two transitional housing facilities (2099 MLK and 156 Fairfield) that were to be rehabilitated as new and expanded transitional housing. During the grant period, in a letter dated November 8, 1999, VORCI requested approval to use one existing facility (438 Frazier Street) for intake and assessment interviews. According to a HUD official, VORCI was also to use the facility to house some of its homeless clients. HUD approved this use on December 22, 1999. Operating funds were approved for these three specific facilities, not to operate existing facilities.

- VORCI charged $18,304 to SHP operating funds for custom-made curtains at the two renovated SHP housing facilities. The Executive Director said that this charge to operating funds was an error and was reimbursed to the Harris House account from the construction account. We confirmed the Harris House account was reimbursed. However, by eliminating the $18,304 cost, total costs charged to SHP operating funds were $18,304 less than the grant funds received from HUD. The total cost of the custom curtains was $52,997, and appeared to be exorbitant and unnecessary. A second payment of $15,689 was also charged to Harris House, but was not classified as an SHP cost and a third payment of $18,304 was paid from the construction account. We observed the housing facilities and found that VORCI also installed mini-blinds with the custom curtains. In our experience, it is not customary and reasonable to provide more than basic window coverings in commercial and Federally subsidized apartments.

- Under supportive service funds, VORCI charged $9,381.25 of duplicate salary costs and $3,011.88 for loan closing costs and late payment fees. The latter two costs were recorded incorrectly as Workman's Compensation and are ineligible.

- Under administration funds, VORCI charged $3,127.08 of duplicate salary costs and $5,405.92 for insurance, membership dues, leasing forms, advertising, stationery, business cards, and late fees. In addition, $2,263.20 for audit costs should have been allocated to other programs. HUD regulations are specific as to eligible uses of administrative grant funds, allowing only costs associated with accounting for the use of grant funds, preparing reports for submission to HUD, obtaining program audits, and other similar costs.

Unsupported Costs

NSS-VORCI did not maintain adequate supporting documentation to show the nature, purpose, and eligibility of numerous expenditures including $313,811 charged to SHP funds. See Appendix C for a detailed listing of unsupported costs.

Documentation for salary and fringe benefit costs did not identify which employees were charged to Harris House accounts and SHP funds. VORCI did not systematically allocate payroll costs to SHP grant categories and other non-SHP activities (see Finding 1). Therefore, we deemed it necessary to estimate eligible salary and fringe benefit costs for each grant category for the purpose of determining if claimed amounts were reasonable.

We estimated eligible salary costs based on several factors including: the ratio of SHP funding to total funding (60 percent), interviews with several VORCI employees, and analyses of total Harris House salaries detailed by employee, which we obtained from a payroll processing company used by NSS-VORCI. Actual salary charges to the SHP included employer payroll taxes of 8.2 percent. Fringe benefit costs (other than employer payroll taxes) included 403b pension costs, and health, life, and worker compensation insurance. VORCI charged fringe benefits totaling $93,604 to Harris House, including $41,191 charged to SHP funds (operating, supportive services, and administrative). Total recorded fringe costs were 8.69 percent of the $1,077,699 in total salaries charged to Harris House per payroll company records. We allocated employer payroll taxes and fringe benefits to our salary estimates at the documented percentages. The following table compares our salary and fringe benefit estimates to VORCI's actual charges to the SHP. Note that we adjusted VORCI's actual charges for errors in salary and fringe costs found by the audit.

	Audit Estimates			VORCI Charges	
SHP Category	Salary	Salary + Taxes	Fringe	Salary and Taxes	Fringe
Operating	$140,544	$152,068	$12,213	$ 18,408.36	$ 2,316.06
Support Svc.	672,987	728,172	58,483	851,855.24	20,431.12
Admin.	88,563	95,825	7,696	43,401.73	18,443.98
Subtotals	902,094	976,065	78,392	$913,665.33	41,191.16
Non-SHP	NA	NA	NA	64,088.89	52,412.79
Totals	$902,094	$976,065	$78,392	$977,754.22	$93,603.95

As shown in the table, our estimates for salary, employer payroll taxes, and fringe costs were greater overall than the amounts charged to SHP funds. The salary and fringe benefit costs charged to the operating and administration grant categories were less than our estimates. Fringe benefit costs charged to support services were also less than our estimates. Therefore, we deemed those salary and fringe charges to be reasonable and eligible. Salaries charged to supportive services exceeded our estimates by $123,683 ($851,855 - $728,172), which we deemed to be unsupported for that grant category. HUD may wish to allow VORCI to reallocate the $123,683 to the operating and/or administration category, within our salary estimates or within amounts budgeted. Note that our salary estimates were made as a test of reasonableness, not to determine eligible costs.

In the payroll company records, VORCI salaries had been charged to two cost centers, Harris House and Veterans Upward Bound. Nearly all employees were charged 100 percent to one program or the other. The Executive Director's salary had been allocated between the two cost centers. However, there was no documented rational for the allocation. The percentage of his salary charged to Harris House steadily increased during the grant period from 32 percent in March 1998 to 70 percent in October 1999 and thereafter. These percentages were unsupported and were not used to charge salary to SHP funds in NSS-VORCI records. However, they demonstrate that NSS-VORCI could have allocated salary costs to SHP cost centers via payroll company record keeping.

Other unsupported or inadequately supported costs charged to SHP funds totaled $190,128. Of this amount, $183,963 was charged to operating funds, $2,400 to supportive services, and $3,765 to administration.

- Under SHP operations, VORCI charged $39,517 for property and other insurance, $38,183 for telephones, $35,245 for office supplies, $27,466 for equipment maintenance, $15,407 for equipment, $12,220 for facility maintenance, and $12,214 for property taxes. It also charged $2,021 for postage (with $445 misclassified as fringe benefits), $793 for utilities, $541 for furnishings, and $356 for grounds maintenance. These expenditures either had no supporting documentation or inadequate documentation to determine whether the costs pertained to the SHP. Charges not related to operation of the three approved SHP facilities would not be eligible. Because VORCI operated other housing facilities and other programs, only a portion of these expenses would benefit the SHP.

- Under supportive services, VORCI charged $2,400 for facility maintenance. This charge was for temporary contract labor, but supporting documentation provided no indication what services were provided, nor what facility was involved. Also, facility maintenance is not an eligible supportive services cost.

- Under administration, VORCI charged $1,669 for work-study employee salaries. Records did not indicate what services they provided. VORCI also charged $778 for postage and postal box rental, and $30 for overnight shipping. Considering the restrictive nature of eligible administrative expenditures, these costs would not be eligible unless VORCI can document that they pertain to administration of the grant.

Eligible Costs and Matching Funds

VORCI expended a total of $1,413,197 for eligible program costs including the $400,000 in rehabilitation costs. VORCI expended $200,314 for eligible operating costs including $32,262 in matching costs we identified during the audit, $777,995 for eligible supportive service costs, and $67,150 for eligible administrative costs. For grant operating funds, HUD regulations require that the grant recipient provide a 25 percent match in the first 2 years and an equal match (50 percent) for the third year. Of the $200,314 of eligible operating expenditures we identified, $133,609, or 67 percent (3-year average of HUD funding), was eligible for funding via the SHP operating grant, and the remaining $66,705, or 33 percent, is VORCI's cost-sharing obligation. Since our audit identified only $32,262 of eligible matching costs not charged to SHP funds, VORCI received $34,443 of excessive, unmatched operating funds. See Appendix D for an analysis of eligible costs and grant funding.

Auditee Comments

"We believe that if provided sufficient opportunity, VORCI can research the alleged ineligible, unsupported and unnecessary costs and prove that substantially all such costs can be justified as being consistent with HUD regulations.

We will need to reconstruct our records by obtaining missing documentation from vendors, demonstrate competitive bidding, show where duplicate charges were subsequently corrected, document necessity/relevance of charges, prove our matching expenditures, etc.

"We propose to research our records as stated above. This review has already begun and will be continued by the Accountant to be retained as noted above. In addition, we are requesting that our auditors (The Wesley Peachtree Group) review our research results and certify its correctness. Any significant differences in the OIG amounts and the certified amounts will be scheduled for repayment to HUD."

OIG Evaluation of Auditee Comments

Both HUD program staff and OIG have given VORCI ample time and opportunity to document its charges to the SHP grant and matching funds. Thus, HUD should impose a time limit for VORCI to submit any further documentation for unsupported costs. Many of the unsupported costs charged to SHP funds or to Harris House (as potential matching costs) are general or administrative in nature and thus may not be allocated solely to the SHP. Since VORCI-NSS did not have an approved cost allocation plan, they will need to provide credible evidence of the benefit to the SHP for general and administrative costs. After more than 4 years from the start of the 1997 SHP grant, statements of recall from VORCI personnel bearing on the purpose and eligibility of costs will not provide reliable evidence. Most general and administrative costs were not budgeted and could overall, if supported, constitute a significant change in fund use. Thus, HUD should consider whether to approve revised fund uses after the fact.

NSS-VORCI should immediately remit $158,330 for ineligible costs identified by this audit. Duplicated costs identified by this audit were duplicated within the spreadsheet of SHP charges prepared by VORCI as support for its use of SHP funds. Thus, each duplicate charge reduces the total costs identified as SHP expenditures to less than the SHP funding received.

Recommendations

We recommend that HUD:

2A. Require NSS-VORCI to repay to HUD $158,330 for ineligible costs.

2B. Require NSS-VORCI to provide adequate support for $313,811 of unsupported costs or repay those costs to HUD.

2C. Require NSS-VORCI to repay to HUD $34,443 for operating grant funds that were not matched. Note that this amount would increase if VORCI provides adequate support for any additional operating costs.

Management Controls

In planning and performing our audit, we considered management and accounting control systems of VORCI to determine our auditing procedures. Our review of management control systems was not performed to provide assurance on the management controls. Management controls include the plan of organization, methods and procedures adopted by management to ensure that goals are met. Management controls include the processes for planning, organizing, directing, and controlling program management.

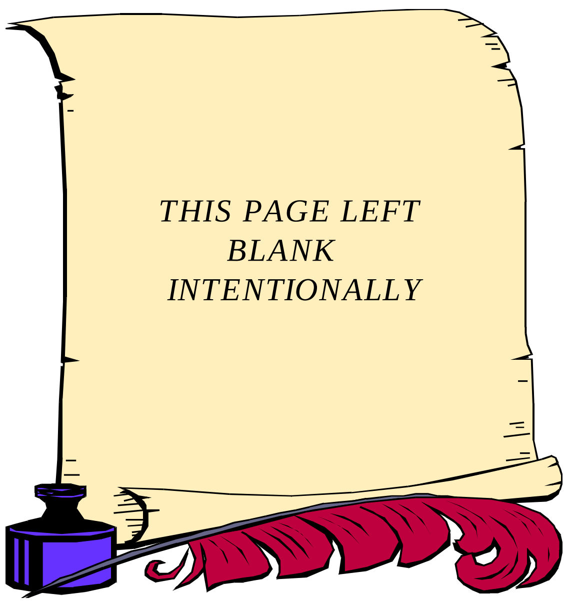
Relevant Management Controls

We assessed the management controls that we determined to be relevant to our audit objectives. We assessed controls pertaining to accuracy of accounting, financial reporting to HUD, and whether expenditures complied with HUD requirements.

Significant Weaknesses

A significant weakness exists if management control does not give reasonable assurance that the entity's goals and objectives are met; that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained, and fairly disclosed in reports.

Significant weaknesses in the controls we assessed are discussed in Finding 1. The control weaknesses were primary causal factors for Finding 2.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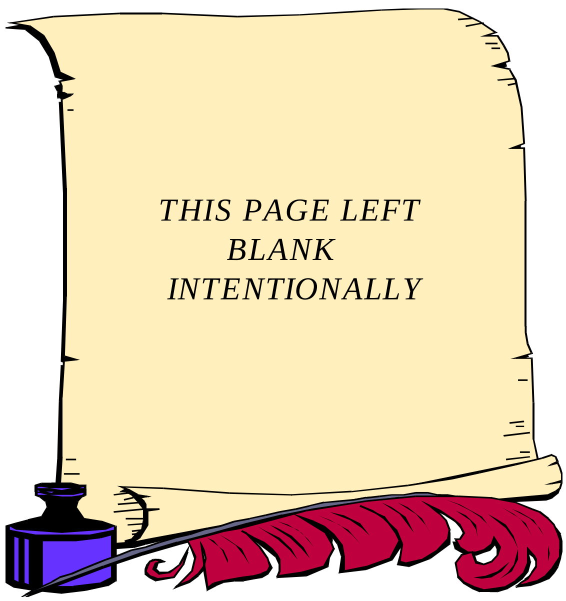
Follow-Up On Prior Audits

This was the Office of Inspector General's first audit of NSS-VORCI. An independent public accountant (IPA) expressed unqualified audit opinions on VORCI's financial statements for the three annual periods ended June 30, 1998, through 2000. Those audits did not identify deficiencies in VORCI's accounting processes and records, nor in its internal controls and compliance with laws and regulations. Our audit noted material deficiencies in NSS-VORCI accounting records, internal controls, budget monitoring, and compliance with HUD requirements for grant and matching fund use (see Finding 1.) We concluded that the IPA's audit opinions could not be relied upon.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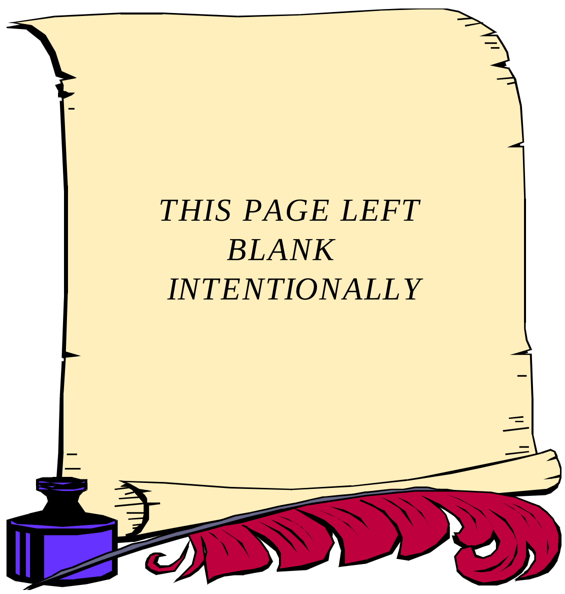
Summary of Questioned Costs

Recommendation No.	Ineligible[1]	Unsupported[2]
2A	$158,330	
2B		$313,811
2C	34,443	
Totals	$192,773	$313,811

1/ Ineligible costs are costs charged to a HUD-financed program or activity that the auditor believes are not allowable by law, contract or Federal, State or local policies or regulations.

2/ Unsupported costs are costs charged to a HUD-financed program or activity and eligibility cannot be determined at the time of audit. The costs are not supported by adequate documentation or there is a need for a legal or administrative determination on the eligibility of the costs. Unsupported costs require a future decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of Departmental policies and procedures.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Schedule of Ineligible Costs

Expenditure Charged As	Operating	Supportive Services	Administration	Comments
Salaries		$ 9,381.25	$ 3,127.08	Duplicate Charges.
Workman's Comp		3,011.88	738.59	Loan closing cost of $2,976, late fee of $35.88, and insurance on storage facility of $738.59.
Legal Fees	18,249.07			Legal Fees re: Conflict with rehab contractor and legal services.
Office Supplies	2,103.63			$594.22 Christmas cards, $45 late fee, and $1,464.41 duplicate charges.
Telephone	23,075.26			ISDN lines of $5,292.14, internet services of $2,249.96, phone system financing of $11,213.45, Community Network Fee of $2000, collection service fee of $551.39, phone bill for non-SHP site of $193.16, and duplicate charges of $1,575.16.
Utilities	3,621.40			Building permits for 971/975 MLK facility of $2,068, power bills for outdoor lighting at 2103 MLK of $705.03, both non-SHP sites, and a duplicate charge of $848.37.
Postage/Mailing Services	239.31		55.00	Late charges for previous bills ($55 and $50.50); and a duplicate charge of $188.81.

Expenditure Charged As	Operating	Supportive Services	Administration	Comments
Printing			2,759.00	VORCI banner and company letterhead and business cards.
Publications			421.56	Advertisements.
Equipment	9007.54			Phone system financing.
Facility Maintenance	11,009.41			$5,959.41 building supplies for a storage shed, $2,450 to relocate fencing, and $2,600 in duplicate charges.
Security Equipment	248.91			Alarm system at storage facility.
Insurance - Not Employee	318.24			Property insurance for 2103 MLK, a non-SHP site.
Membership Dues	672.00		777.12	National Center for Nonprofit Boards membership ($672), and other association memberships, forms and assessments ($777.12).
Subscriptions	39.95		154.65	Subscription to NonProfit Times ($39.95), real estate advertisement and check order ($154.65).
Property Taxes	1,332.33			Property taxes for 2103 MLK, a non-SHP site.
Furnishings	18,303.95			Custom curtains charged to construction funds, erroneously listed as operating cost. Cost also deemed unnecessary.

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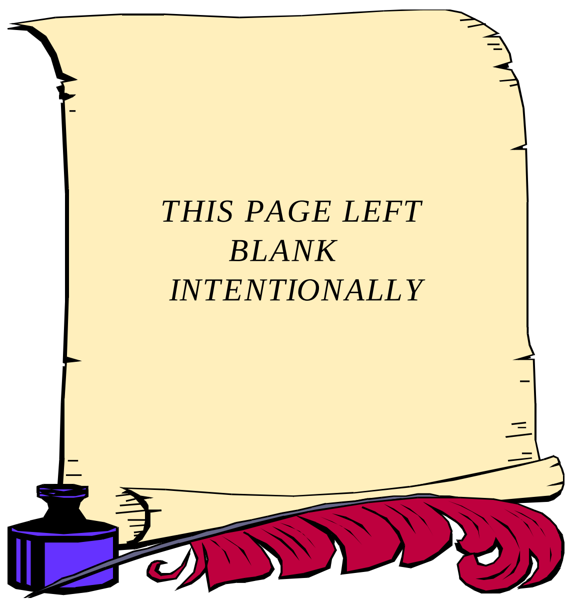
Expenditure Charged As	Operating	Supportive Services	Administration	Comments
Admin. Expenses			500.00	IRS Determination Letter fee.
Accounting Fees			2,263.20	Pro-rata non-SHP share of audit expense.
Unapproved Costs charged to various accounts.	46,920.16			Costs for existing non-SHP housing and office facilities.
Total Ineligible Costs[1]	$135,141.16	$12,393.13	$10,796.20	
Unmatched Grant Funds	34,442.53			
Total Ineligible for Funding	$169,583.69	$12,393.13	$10,796.20	

1/ Total for all categories $158,330.49.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Schedule of Unsupported Costs

Expenditure Charged As	Operating	Supportive Service	Administration	Comments
Salaries		$123,683.10	$1,669.26	Unsupported salaries ($123,683.10). Payments for Work Study employees ($1,669.26).
Fringe Benefits	$445.28			Postage charged to Fringe Benefits.
Office Supplies	35,245.40			Office supplies, printers, scanners, computers, and other miscellaneous charges.
Telephone	38,182.79			Long distance charges, office phone lines, telephone maintenance contract payments, and other miscellaneous charges.
Utilities	793.49			Power and gas bills for undocumented sites.
Postage	1,576.18		778.00	Postage ($1,576.18). Postage and Post Office Box rental ($778).
Mailing Services			30.13	Overnight shipment.
Equipment	15,406.69			Mail meter lease payments, copier lease payments, maintenance contract payments on equipment, and other miscellaneous charges.

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Expenditure Charged As	Operating	Supportive Service	Administration	Comments
Equip. Maintenance	27,465.51			Lock repair, additional mail meter, copier and phone system leases, maintenance contract payments, and other miscellaneous charges.
Grounds	355.68			Landscaping material for undetermined location.
Facility Maintenance	12,219.50	2,400.00		Building supplies and labor payments for maintenance or repairs at undocumented locations, and other miscellaneous charges ($12,219.50). Temporary employee for undocumented work ($2,400).
Insurance – Not Employee Related	39,517.23		1,287.52	Office, undetermined property, and auto insurance.
Property Taxes	12,214.02			Property taxes for undocumented site and vehicle registration renewal for undetermined vehicles.
Furnishings	541.21			Business furniture with inadequate documentation.
Total Unsupported Costs[1]	$183,962.98	$126,083.10	$3,764.91	

1/ Total for all categories $313,810.99.

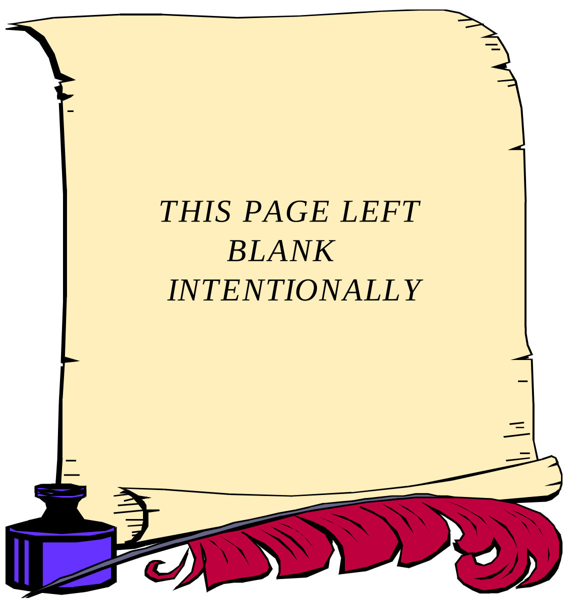
Analysis of Eligible Costs and Grant Funding (excluding Rehabilitation Funds)

	Operating	**Supportive Service**	**Administrative**	**Total**
Charged to SHP	$509,825.00	$888,258.00	$ 87,255.00	$1,485,338.00
Less:				
Ineligible	(135,141.16)	(12,393.13)	(10,796.20)	(158,330.49)
Unsupported	(183,962.98)	(126,083.10)[1]	(3,764.91)	(313,810.99)
Misclassified	(28,284.48)	28,284.48		
	5,615.38	727.12	(6,342.50)	
		(798.41)	798.41	
Eligible Costs	$168,051.76	$777,994.96	$ 67,149.80	$1,013,196.52
Matching Costs	32,261.93	NA	NA	32,261.93
Subtotal	$200,313.69			
HUD Share	x .667[2]			(66,704.46)
Eligible Funding	$133,609.23[3]	$777,994.96	$ 67,149.80	$ 978,753.99

[1] This amount includes $123,683.10 in salaries exceeding our cost estimate. HUD may wish to allow reallocation of these salaries to the Operating and Administration categories where our salary estimates were higher.

[2] The 3-year average 66.7 percent HUD share was after the required match (75 percent, 75 percent, and 50 percent per year, respectively) The $66,704.46 is NSS/VORCI's cost share (33.3 percent).

[3] The difference between eligible operating costs and eligible operating funding is $34,442.53 of unmatched expenditures that must be repaid. This amount would increase if VORCI provides HUD with support for, and HUD allows, additional operating costs.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Auditee Comments

July 1, 2002

DELEIVED BY ELECTRONIC MAIL AND USPS RESGISTERED MAIL

Ms. Nancy H. Cooper, *Regional Inspector General for Audit Southeast/Caribbean*
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
Region IV Office of the Inspector General
Office of Audit
Richard B. Russell Federal Building
75 Spring Street, SW, Room 330
Atlanta, Georgia 30309

Dear Ms. Cooper:

Enclosed is our formal response to the recent audit that you conducted of the 1996 and 2000 Supportive Housing Grants received by NSS-VORCI. The Board of Directors of both entities, NSSFNS, the parent Corporation and its subsidiary VORCI, fully recognizes the gravity of these findings and particularly any alleged abuse of funds by an individual. In developing our response we have consulted with our attorneys and our independent auditors, the Wesley Peachtree Group, CPA. As you review our response, there are several matters that we want to make abundantly clear.

- Since inception of the SHP grants, we have exceeded our program goals in serving the number of homeless veterans. Over 1,200 veterans have been served over the past three years. Our program has received several citations as an exemplary program in serving the needs of veterans.

- None of the SHP funds received have gone to personally enrich anyone at NSS-VORCI. All funds have been used to advance the programmatic cause of providing supportive housing for Atlanta's homeless veterans.

- We have not purposely operated the programs inconsistent with the SHP requirements. We tried our best to establish the proper accounting systems, hire qualified personnel and follow the program regulations. We completed timely external audits and those audits revealed that we were on the right track.

Ms. Nancy H. Cooper, *Regional Inspector*
General for Audit Southeast/Caribbean
U.S. DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT
July 1, 2002
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- Lastly, the Board of Directors (and the Executive Director) are committed to doing all that is necessary to maintain our current programs and the U.S. Department of Housing and Urban Development continued support. We have crafted a corrective action plan that we believe addresses the matters raised in your audit. We ask for your input and comments.

Should you have any question(s) as you review the enclosed material, please do not hesitate to contact either one or both of us.

Very truly yours,

//S//	//S//
Geoffrey A. Heard	Percy D. Butler
President & CEO	President, Board of Directors
NSSFNS, Inc.	VORCI

BOD/db

cc: Board Files

Enclosure(s):

VETERAN'S OPPORTUNITY AND RESOURCE CENTER, INC. (VORCI)

RESPONSE TO DRAFT HUD OIG AUDIT DATED MAY 10, 2002

General Comments

The NSS-VORCI housing program is a direct outgrowth of the need to provide supportive housing services for Atlanta's homeless veterans. Almost half of Atlanta's homeless population is estimated to be armed services veterans. From a six room framed house over twelve years ago, VORCI has expanded its housing program to include the Harris House Veterans Center, Harris House Transitional Apartments and Harris House Stabilization Center, accommodating as many as 35 veterans (male and female) at any given time.

Our program has been extremely successful and, overall, has accomplished the programmatic funding goals we promised to our sponsors, including the U.S. Department of Housing and Urban Development.

During the three short years we have operated these facilities, we have assisted more than 1,200 veterans and their families receive independent housing of some sort. We have seen residents move from a state of homelessness to homeownership in two (2) years or less. There have been twenty-nine (29) individuals to purchase homes after completing our transitional apartment program and thirty-four (34) persons have moved into unsubsidized apartment living and twenty-seven (27) have re-united with their families. This is a transitional housing program; therefore, residents sign a two-year license agreement to participate in the program. They agree to develop an ISS that will address their academic, social and employment needs with home ownership as the ultimate aim.

1

VETERAN'S OPPORTUNITY AND RESOURCE CENTER, INC. (VORCI)

RESPONSE TO DRAFT HUD OIG AUDIT DATED MAY 10, 2002
(Continued)

In 1999, VORCI was approached by the owner of the property at 438 Fraser St., SE, and the Board President of the former Imperial Welcome House, a housing facility for Atlanta's working poor, and was asked to operate the facility as a housing stabilization center for the existing population and those persons we would place in the facility. At the urging of the City of Atlanta and the State Department of Community Affairs, we agreed to this request and took over operation of this facility. During the ensuing months we worked with the people we inherited and were successful in moving them into independent living situations. We saw people address legal matters, rectify outstanding arrest warrants, become engaged and get married as well as obtaining career oriented employment.

We have established collaborative relationships with the VA Hospital, the Salvation Army Lodge, and the Task Force for the Homeless and the Homeless Action Group so that qualified applicants can be referred to us through local area service providers for assistance.

Unfortunately, as with many small nonprofit agencies, our outstanding programmatic success has come at the expense of not being able to afford the resources necessary to invest in a top-notch administrative infrastructure. We have diligently tried. However based on your report, we have considerable shortcomings in our fiscal management area. Our spin-off from NSSFNS into a separate subsidiary (VORCI) in October 2000 was done solely to focus on our core business of providing supportive housing to homeless veterans. We set up written polices and procedures, a new accounting system (Peachtree Accounting) and hired a new accountant to manage our fiscal affairs. Our systems have been audited twice by our external auditors and they have determined us to be substantially in compliance with applicable regulations governing the SHP requirements.

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VETERAN'S OPPORTUNITY AND RESOURCE CENTER, INC. (VORCI)

RESPONSE TO DRAFT HUD OIG AUDIT DATED MAY 10, 2002 *(Continued)*

Finding 1:

Management did not responsively manage grant funds, accounting and compliance with SHP requirements. Accounting for SHP expenditures and receipts was incomplete and inaccurate. Salary and other costs benefiting multiple programs were not properly allocated. Expenditures significantly deviated from the approved SHP budget.

Recommendations: *Terminate further SHP grant funding to VORCI. VORCI should not be considered for new funding until its Board of Directors and Executive Director have established written procedures and controls to ensure accounting is complete and accurate, and expenditures are monitored for eligibility, need and correlation to the budget. VORCI should also demonstrate complete and accurate accounting for its activities before new grants are considered.*

Require that VORCI replace its Executive Director and strengthen Board oversight processes before considered further grant funding.

Response: The accounting system in place at VORCI during the OIG audit was initially established by National Scholarship Service, (the Parent Corporation also known as NSSFNS). From the beginning until NSS transferred accounting responsibility to VORCI in October 2000, NSS used its best efforts to ensure that all SHP funds were accounted for and categorized properly. VORCI continued the NSS accounting system through the OIG audit report. On several occasions, NSS and VORCI provided information to HUD on various aspects of the SHP funds utilization and accounting, and adopted changes requested by HUD to the same. We acknowledge below that our Accountants may have made mistakes. It is important to note, however, that neither NSS nor VORCI intentionally adopted an accounting system that violated SHP requirements, nor were any SHP funds misappropriated.

NSS and then VORCI accounted for the SHP funds in one particular cost center: Harris House Veteran's Center. Although our accounting system has the capability of tracking SHP expenditures by category (operating, supportive service and administration), unfortunately our Accountant did not complete the set up of the general ledger chart-of-accounts in this fashion. Instead, our Accountant maintained such information using MS Excel spreadsheets. Consequently, we did have expenditure classification issues among the SHP budget categories. However, we did not overspend the SHP grant nor did we spend any SHP funds on any non-SHP activities.

VORCI did establish a system of allocating employee salaries among our various programs. Salaried employees are initially charged to the programs based on percentage of time spent, however, our system does not involve a periodic formal confirmation of the percentage of time spent on each activity. The Accountant was charged with assuring that the allocations were consistent and properly charged to the SHP grant categories.

We have used our external auditors to assist us with identifying the year-end adjusting journal entries, such as recording security deposit liabilities, accounts payable, cash receipts classifications, etc. The OIG auditors may not have taken these adjustments into account during their audit. As we most recently found, our Accountant was not experienced with accrual basis accounting but was primarily maintaining the general ledger on the cash basis of accounting.

VORCI should have done a much better job in tracking budget-to-actual expenditures for the SHP budget categories. We should have been in a better position to obtain prior approval for budget revisions. This condition is a direct result of our accounting for SHP expenditures in total rather than by the grant categories.

We have identified sufficient matching funds to satisfy the matching requirements for SHP grant. For example, for the years ended June 30, 2001, 2000, 1999 and 1998, we had $426,570, $303,524, $825,518 and $739,571, respectively of available matching funds. These amounts are well in excess of the required matching amounts. Unfortunately, our accounting system did not specifically identify and classify the expenditures as "SHP matching expenditures", however our records do identify the expenditures and we can provide specific (and sufficient) expenditure details to justify the match.

With regard to the alleged abuse of funds comment, (the $23,976 of questionable credit card charges by the Executive Director), the VORCI Executive Committee has initiated its own review of these transactions. In this regard, members of the Executive Committee that have accounting and auditing skills and these skills will be utilized to determine the propriety or impropriety of the credit card transactions. A full written report will be submitted to the Board of Directors with recommendations on correcting any wrongdoing, including the termination of the wrongdoers, if any.

The Executive Committee will also revisit the issues surrounding the short-term loan from a Board member to VORCI. While the loan was made and approved in good faith to address an immediate financial emergency, we nonetheless will consider corrective action in view of the issues raised by the OIG.

Corrective Action: VORCI will revisit its general ledger chart-of-accounts to be sure sufficient accounts are established to permit classification of expenditures by SHP budget categories. Our revised system will include posting the HUD approved budget line items so that we can monitor budget compliance. The OIG has indicated that our Peachtree Accounting software is adequate provided that it is properly maintained. VORCI will also establish a cost allocation plan to ensure all direct costs are properly allocated and all indirect costs are allocated using an acceptable methodology. To solve the matching funds requirement, we will establish specific general ledger accounts for the SHP grant entitled "SHP matching funds" in which we will post our various matching expenditures consistent with HUD regulations. This will provide an unquestionable audit trail of our matching funds.

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We will move expeditiously to hire a more experienced accountant with specific nonprofit grants accounting experience, preferably with five or more years of field experience.

The Executive Committee will investigate the abuse of funds referenced in the OIG audit and issue written recommendations to the Board of Directors. The written report will be shared with OIG and HUD.

As for future compliance, we will modify our corporate by-laws to establish a standing audit and finance committee to strengthen the Board of Directors' oversight of fiscal management and audit resolution. In keeping with our existing five-year action plan, we have already increased the size of the Board of Directors and filled the vacant positions with persons with more fiscal experience.

As evidence of our compliance, we have requested that our auditors (The Wesley Peachtree Group), who have significant nonprofit and governmental grants experience, provide a certification to HUD of our accounting system compliance within six (6) months.

***Finding 2*:**

NSS-VORCI expended SHP funds for ineligible, unnecessary and unsupported costs.

Recommendations: *Require NSS-VORCI to repay to HUD, $253,596 for ineligible costs and $18,304 for unnecessary costs. Note that the $18,304 unnecessary cost also duplicated charges to construction funds.*

Require NSS-VORCI to provide adequate support for the $200,241 of unsupported costs or repay those costs to HUD.

Require NSS-VORCI to repay to HUD, $34,443 for operating grant funds that were not matched. Note that this amount would increase if VORCI provides adequate support for any additional operating costs.

Response: We believe that if provided sufficient opportunity, VORCI can research the alleged ineligible, unsupported and unnecessary costs and prove that substantially all such costs can be justified as being consistent with HUD regulations. We will need to reconstruct our records by obtaining missing documentation from vendors, demonstrate competitive bidding, show where duplicate charges were subsequently corrected, document necessity/relevance of charges, prove our matching expenditures, etc.

Corrective Action: We propose to research our records as stated above. This review has already begun and will be continued by the Accountant to be retained as noted above. In addition, we are requesting that our auditors (The Wesley Peachtree Group) review our research results and certify its correctness. Any significant differences in the OIG amounts and the certified amounts will be scheduled for repayment to HUD.

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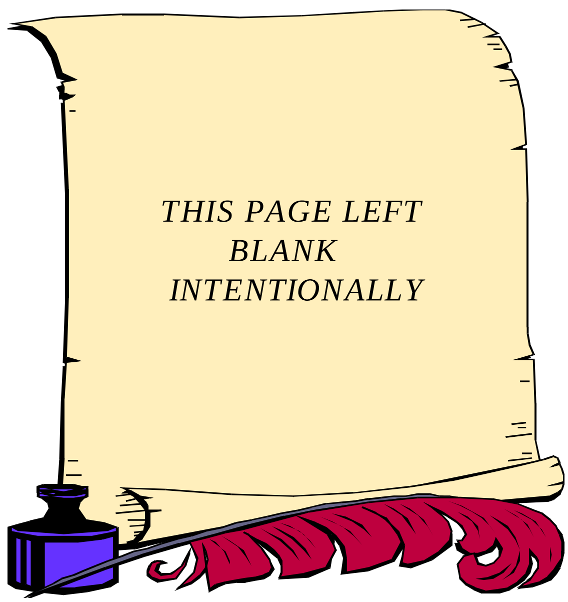
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