AUDIT REPORT

SPANISH VILLAGE
COMMUNITY DEVELOPMENT CORPORATION

UPFRONT GRANT AND HOME LOAN

HOUSTON, TEXAS

2003-FW-1004

APRIL 28, 2003

OFFICE OF AUDIT, REGION 6
FORT WORTH, TEXAS

Issue Date
April 28, 2003
Audit Case Number
2003-FW-1004

TO: Alvin E. Braggs,
Director, Fort Worth Multifamily Property Disposition Center, 6AHMR

E. Ross Burton
Director, Multifamily Housing Division, 6AHM

Katie S. Worsham
Director, Community Planning and Development, 6AD

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FROM: D. Michael Beard
Regional Inspector General for Audit, 6AGA

SUBJECT: Citizen's Complaint
Upfront Grant and HOME Loan
Spanish Village Community Development Corporation
Houston, Texas

In response to a citizen's complaint, we conducted a limited scope audit of the Upfront Grant and the HOME Loan provided to the Spanish Village Community Development Corporation (SVCDC). The complaint alleged wrongful expenditures of government funds, violations of the grant and loan agreements, failure by HUD and the City of Houston to follow Upfront Grant and HOME loan guidelines, and political influence that prevented HUD from declaring the SVCDC in default of the agreements. Our primary objective was to determine whether the allegations were valid.

We concluded there were wrongful and unsupported expenditures, violations of the grant agreement terms by the Spanish Village Community Development Corporation, and a general failure by HUD and by the City of Houston Housing and Community Development Department (HCDD) to take timely remedial action as permitted by the Upfront Grant and HOME loan agreements. However, HUD did take remedial action and declared a default under the grant agreement on March 12, 2003.

Our report contains one finding with recommendations requiring action by your offices. In accordance with 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.

Should you or your staff have any questions, please contact Jerry R. Thompson, Assistant Regional Inspector General, at (817) 978-9309.

Executive Summary

In response to a citizen's complaint, we conducted an audit of the Upfront Grant and the HOME Loan provided to the Spanish Village Community Development Corporation (SVCDC). The complaint alleged wrongful expenditures of government funds, violations of the grant and loan agreements, failure by HUD and the City of Houston to follow Upfront Grant and HOME loan guidelines, and political influence that prevented HUD from declaring the SVCDC in default of the agreements. Our primary objective was to determine whether the allegations were valid. Specifically, our objectives were to determine whether: (1) there were wrongful expenditures of government funds by any party involved in the SVCDC renovation project; (2) the SVCDC's performance complied with its agreements; (3) HUD executed and monitored the sale and Upfront Grant properly and in accordance with guidelines, (4) the City of Houston complied with its obligations for monitoring the HOME loan, and (5) there was political influence or involvement that limited HUD's ability to ensure completion of the renovations.

The citizen's complaints were partially valid.

We concluded that several of the citizen's allegations were valid. We found more than $90,500 of ineligible and unsupported expenses charged to a federal loan. We also found that, possibly because it lacked administrative capacity to complete the renovations, the Spanish Village Community Development Corporation (SVCDC) violated grant and loan agreements and could not even start the renovations until long after the renovations were supposed to be completed. Neither HUD nor the City of Houston Housing and Community Development Department (HCDD) had a plan for ensuring completion of the renovation project even after the project was more than 4 years overdue. SVCDC finally completed the first phase of the renovations during January 2001; however, the renovations did not meet HUD standards and the renovations ceased again with no restart date planned. As a result, the residents of the Spanish Village Apartments continued to live in substandard units. Finally, we were unable to substantiate any undue political influence.

On March 12, 2003, the HUD Multifamily Office in Fort Worth declared a default under the Upfront Grant Agreement. In the default letter, HUD gave SVCDC two options to dispose of the property. SVCDC could, within 60 days: (1) sell the property to a nonprofit entity with the capacity and experience to complete the rehabilitation and assign the remaining grant funds to that entity or (2) deed the property back to HUD.

Recommendations.

We are recommending that HUD continue with its remedial action by establishing an acceptable plan of action with time frames to complete alternative measures to obtain and complete renovations to the property if SVCDC does not comply with HUD's options detailed in the default letter of March 12, 2003. Also, HUD needs to de-obligate the balance of SVCDC's Upfront Grant or assign the balance of the Grant to an acceptable owner who has the capacity to bring the property up to HUD Standards. We further recommend that HUD require the City to repay the $90,500 of ineligible or unsupported costs paid from the HOME loan. Finally, if HUD terminates the project under SVCDC, we are recommending that HUD require the City of Houston to repay the $245,228 that SVCDC expended on the project and de-obligate the full $498,000 of the HOME loan, as HUD requires for projects terminated without completion.

We provided a draft of this report to the SVCDC's Board of Directors and HUD's Multi-family and Community Planning and Development staff on March 24, 2003. We held an exit conference with the SVCDC on April 10, 2003. SVCDC provided written comments at the exit conference. We included paraphrased excerpts of their comments in the finding and included the complete written response in Appendix B.

The SVCDC representatives did not dispute the facts of the audit, however, they felt the audit was unnecessarily critical of the SVCDC. The SVCDC believed its Board of Directors that existed prior to January 2002 and the Board of Directors that currently exists should be considered as separate entities because the Boards are composed of different members. Therefore, the SVCDC believed that the actions of the previous board of Directors should be considered as separate from the current Board of Directors. The SVCDC claimed that most of the problems found during our audit were associated with the previous Board of Directors.

We believe the SVCDC is a single entity, no matter who sits on its Board of Directors. SVCDC's comments did not change our position.

Table of Contents

Abbreviations

CFR	Code of Federal Regulations
CHDO	Community Housing Development Organization
FHA	Federal Housing Administration
HCDD	City of Houston Housing and Community Development Department
HOME	HOME Investment Partnership Act
HUD	U. S. Department of Housing and Urban Development
OIG	Office of Inspector General
SVCDC	Spanish Village Community Development Corporation

Introduction

Background

Spanish Village Apartments is a 126-unit apartment complex located at 4000 Griggs Road, Houston, Texas 77021. HUD sold the Spanish Village Apartments to the Spanish Village Community Development Corporation (SVCDC), a resident nonprofit group on September 30, 1996, for $1. HUD provided an Upfront Grant of $2,266,445 in September 1996 for the repair and renovation of the Spanish Village Apartments. The Upfront Grant Agreement required the repairs to be completed by September 1998. The City of Houston provided an additional $498,000 through a HOME Loan in May 1997 to rehabilitate the property.

SVCDC spent $788,735 of the Upfront Grant between October 31,1997 and August 30, 2001, leaving a $1,477,710 balance in the Upfront Grant account. SVCDC spent $245,228 of the HOME loan funds between December 17, 1997 and October 17, 2001, leaving a balance of $252,772 in the HOME loan account. The City of Houston has not processed a HOME loan draw since October 2001 and the Multifamily Office in Fort Worth has not allowed SVCDC an Upfront Grant draw since August 2001.

The Houston HUD Multifamily Office formed a development team to implement the renovation project and selected the Carver Institute (headed by Dr. Alvin I. Thomas) to be the lead member of the team on June 11, 1997. SVCDC had previously hired the Carver Institute to serve as the management agent for the Spanish Village Apartments and entered into a management agent contract with Dr. Thomas on January 1, 1996. SVCDC also hired the Carver Institute as the developer for the renovation project and entered into a developer contract with Dr. Thomas on January 1, 1997. HUD assigned all properties handled by the Houston Office to the Fort Worth Property Disposition HUB as part of a larger HUD reorganization. After April 1998, the Houston Multifamily Office no longer wrote Upfront Grants.

Under the Upfront Grant Program (Grant), HUD may provide grants and loans for rehabilitation, demolition, rebuilding, and other related development costs as part of the disposition of a HUD-owned multifamily housing project. HUD must make a determination that a grant or loan would be: more cost-effective than project-based rental assistance; economically viable on a long-term basis; and preserve affordable rental housing in a tight rental market. Overall, the purpose of multifamily disposition is to dispose of projects in a manner that will protect the financial interests of the federal government and be less costly to the federal government than other reasonable alternatives by which HUD can further the goals of:

- Preserving units so that they are available to and affordable by low- and moderate-income persons;
- Preserving and revitalizing residential neighborhoods;
- Maintaining the existing housing stock in a decent, safe, and sanitary condition;
- Minimizing the involuntary displacement of residents;
- Minimizing the need to demolish projects; and
- Maintaining projects for the purpose of providing rental or cooperative housing.

Under the HOME Investment Partnership Act (HOME), the City funds a variety of programs, including rehabilitation of multifamily rental housing, Community Housing Development Organization (CHDO) operating expenses and program administration. HOME is an entitlement program in which HUD provides funds to cities or states for the purpose of expanding the supply of decent, safe, sanitary, and affordable housing for very low- and low-income Americans. HUD began providing HOME funds to the City of Houston in 1994.

Audit Objectives

We limited our overall audit objective to determining whether the allegations were valid. Our specific audit objectives were to determine:

- Whether there were wrongful expenditures of government funds by any party involved in the SVCDC renovation project;

- Whether the SVCDC's performance complied with its agreements with HUD;

- Whether HUD executed and monitored the sale and Upfront Grant Agreements properly and in accordance with its agreements with SVCDC;

- Whether the City of Houston Department of Housing and Community Development complied with its obligations for monitoring the HOME Loan; and

- Whether there was political influence or involvement that limited HUD's ability to ensure completion of the renovations.

Audit Scope and Methodology

We conducted our fieldwork between May 2001 and March 2003 at Spanish Village Apartments at 4000 Griggs Road, Houston, Texas, at the HUD Multifamily Office at 2211 Norfolk, Houston, Texas, and at the HUD Multifamily Office at 801 Cherry Street, Fort Worth, Texas.

To accomplish our objectives, we interviewed the complainant, various HUD personnel, current and former Board members of the SVCDC, the Spanish Village Apartments manager, current and former employees of the City of Houston, the architect, and the accountants and attorneys for SVCDC. We examined records provided by HUD, the SVCDC, the apartment management, the accountants, the bank, and documents provided by the complainant. We also inspected the project.

During the records examination, we reviewed evidence supporting 100 percent of the federal funds drawn for the renovations between September 1996 and September 2001. We were unable to verify nonfederal funds including rents, fees, etc. that SVCDC collected from the tenants and used for operations at the Spanish Village Apartments because SVCDC did not keep adequate records.

This was a limited scope audit and covered the period September 30, 1996, through March 12, 2003. We conducted our audit in accordance with generally accepted government auditing standards.


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Spanish Village Community Development Corporation Defaulted on its Grant and Loan Agreements

The Spanish Village Community Development Corporation (SVCDC) has not completed HUD-funded renovations on the Spanish Village Apartments more than 4 years after it was supposed to complete those renovations. A 1996 Sales Contract between HUD and SVCDC and a 1997 HOME Loan Agreement between the City of Houston and SVCDC required that SVCDC complete renovations by September 1998. Also, SVCDC expended about $90,500 in HOME Loan funds for ineligible or unsupported activities. SVCDC did not complete the renovations because it did not have the administrative capacity to complete the project in accordance with its agreements with HUD. As a result of SVCDC's inability to complete the renovations, completion of the project is doubtful and Spanish Village residents have continued to live in substandard conditions.

Criteria: Sales Contract and Special Warranty Deed

The Sales Contract and Special Warranty Deed control SVCDC's responsibilities for renovating the Spanish Village Apartments. Paragraph (1) of Rider 7 of the Sales Contract requires SVCDC to rehabilitate the property by September 30, 1998, which is "within twenty-four (24) months from the date of this Deed" (September 30, 1996). Paragraph (6) of Rider 7 allows HUD to reclaim the property in case of default, "If Grantee fails to comply with (paragraph 1), above…Grantor and his successors in office shall be entitled to exercise any available remedies including the right to enter and terminate the estate hereby conveyed."

The first two paragraphs of Rider 11 "Resident Initiatives Development Plan" require the SVCDC to "(Maintain a) democratically elected Board of Directors and officers…in accordance with the organization's by-laws" and to "Provide a training program available to all residents which would prepare residents to assume all responsibilities of ownership and to administer a professional property management contract…." The Special Warranty Deed provides the same such requirements as the Sales Contract.

Criteria: Upfront Grant Agreement

Article V of the Upfront Grant Agreement requires SVCDC "…to complete the Repairs within 24 months after closing." The date of the Sales Contract and the Special Warranty Deed is September 30, 1996; therefore, the repairs should have been completed by September 30, 1998. Paragraph D of Article XV of the Upfront Grant Agreement allows HUD several default remedies. These remedies include: canceling or revising budget line items; suspending payments; assigning the grant to a mortgagee or third party; recapturing improperly expended funds; terminating the grant; or other available and equitable remedial actions.

Criteria: 24 CFR 92 "HOME" Program

According to 24 CFR 92.205, paragraph e., "A HOME assisted project that is terminated before completion, either voluntarily or otherwise, constitutes an ineligible activity and any HOME funds invested in the project must be repaid to the participating jurisdiction's HOME Investment Trust Fund…" Paragraph a. of 24 CFR 92.504 states, "The participating jurisdiction is responsible for managing the day to day operations of its HOME program, ensuring that HOME funds are used in accordance with all program requirements and written agreements, and taking appropriate action when performance problems arise." Paragraph d. of 24 CFR 92.206 allows reasonable and necessary soft costs associated with the rehabilitation of HOME assisted projects.

The Houston Multifamily Office failed to ensure that SVCDC had the capacity to complete the project.

From the beginning, the Houston Multifamily Office did not properly qualify the project. It conducted initial negotiations with SVCDC informally (without a document trail), failed to consider existing agreements between SVCDC and other entities, and prepared an incomplete and inaccurate Grant Agreement.

There was no documentation showing how the Multifamily Office in Houston determined that the Carver Institute had the capacity to head a development team and to train SVCDC's Board of Directors to manage the project after the renovations.

There was no documentation showing that the Houston Multifamily Office had reviewed all of the agreements between SVCDC and the management agent. For example, the Houston Multifamily Office either did not know or did not care that the management agent's contract contained some unusual provisions. These provisions allowed the agent to collect certain funds without accounting for them, keep interest received on security deposits, keep returned check fees, etc.

During our review of the Upfront Grant Agreement, we found that the Multifamily Office in Houston miscalculated the total renovations estimate in both the original and revised Form HUD-9552 portions of the Grant Agreement. These were mathematical errors that would probably have been caught if the Houston Multifamily Office had an effective review process. The Houston Multifamily Office understated the estimated cost on the original Form HUD-9552 by $271,613 or almost 12 percent of the amount of the Upfront Grant ($271,613 divided by $2,266,445 equals 11.98 percent). The Houston office also understated the revised estimated cost by $40,000 or almost 2 percent of the amount of the Upfront Grant. Therefore, SVCDC agreed to undertake a renovation project that was based on an understated budget.

The Form HUD-9552 is also known as the "Post-Closing Repair Requirements" and is a list of items that HUD says must be completed as part of the renovations. The form provides HUD's estimate of the needed repairs and an estimate of the cost of each repair. It specifically states that the purchaser (SVCDC) is responsible for creating its own cost estimate.

The Upfront Grant Agreement also referred to a "Sources and Uses of Funds Statement" which was supposed to be Exhibit B of the Agreement. Our review of the Agreement showed that there was no Exhibit B or "Sources and Uses of Funds Statement." Without the statement, HUD had to rely on the "Post-Closing Repair Requirements" document to control SVCDC's usage of the grant funds.

SVCDC continuously demonstrated its inability to complete the project.

Throughout the project, SVCDC demonstrated that it did not have the capacity to complete the project. Specifically, SVCDC:

- Did not plan the project well;
- Violated procurement rules;
- Relocated tenants without HUD approval;
- Prepaid the architect and developer;

- Fought with residents and contractors;
- Failed to complete Phase I renovations properly; and
- Implemented inappropriate compensation for its Board of Directors.

Because of SVCDC's lack of capacity, the renovations were not completed on time. Subsequently, Spanish Village residents have continued to live in substandard housing more than 4 years after the project was supposed to be completed.

SVCDC did not plan the project well.

The SVCDC hired Future Management and Consultants to serve as the construction manager and signed a construction management contract with Mr. Arvie Jones on August 1, 1997. SVCDC's Board of Directors decided to terminate the construction management contract on September 9, 1999, because it believed that the construction manager contract would duplicate work performed by the architect/engineer, the general contractor, the project manager for the City of Houston, and other trade inspectors on the job.

SVCDC violated procurement rules.

SVCDC hired Ice Makers Inc. (d.b.a. SuperCool Mechanical & Construction Contractors) as the General Contractor and signed a contract with Mr. Don Adams on September 3, 1997. The Fort Worth Multifamily Office instructed SVCDC to terminate the contract with SuperCool and re-bid the contract because SVCDC did not comply with the competitive bidding provisions of the Grant Agreement or obtain HUD approval for significant changes in the scope of work under that contract. SVCDC terminated the Ice Makers contract and entered into a new general contractor contract with Roca Construction Company (Mr. Roy Owens) on January 27, 2000.

SVCDC incurred over $90,500 of ineligible and unsupported expenses from the HOME loan.

In November, 1997, SVCDC paid $86,299 to bond and insure SuperCool. SuperCool never performed the renovation work. Applicable cost principles for the City, Office of Management and Budget Circular A-87, provide basic guidelines for allowability of program costs. To be allowable under Federal awards, the costs must be necessary and reasonable for proper and efficient performance and administration of Federal awards. Since the program did not receive renovation work from

SuperCool, these costs are not necessary and reasonable and are, therefore, ineligible. Both SVCDC and the City of Houston have been unable to recover the bond and insurance. According to 24 CFR 92.504, paragraph a., the Participating Jurisdiction (the City of Houston) is responsible for ensuring HOME funds are used in accordance with all program requirements.

SVCDC effectively paid an additional unsupported $4,210 to HCDD. On November 6, 1997, HCDD advanced SVCDC $134,315 on its HOME loan. On December 17, 1997, HCDD drew $138,525 from the HOME loan account to repay itself for the advance. Despite multiple requests, HCDD did not explain why it withdrew $4,210 more from the HOME loan account than it gave to SVCDC.

SVCDC relocated tenants without HUD approval.

In approximately April 1998, SVCDC relocated 28 tenants to other apartment complexes in preparation for the first phase of the Spanish Village renovations. SVCDC only planned the relocations to last for 2 months; however, SVCDC still had not provided acceptable renovation plans and specifications to HUD. The plans that SVCDC had provided went far beyond those renovations authorized by the Upfront Grant Agreement and the Fort Worth Multifamily Office would not approve them. Since the Fort Worth Office could not approve the plans, the relocations that SVCDC planned for 2 months actually lasted for 43 months.

SVCDC prepaid the architect and developer.

Also, during April 1998, HUD assigned all properties handled by the Houston Office to the Fort Worth Property Disposition HUB as part of a larger HUD reorganization. After April 1998, the Houston Multifamily office no longer wrote Upfront Grants. By the time HUD transferred responsibility for Upfront Grants to the Fort Worth office, SVCDC had already paid $93,600 in payments to the architect and $57,371 to the developer although SVCDC had not provided any acceptable plans and specifications to either HUD or the City of Houston. Fort Worth Multifamily office representatives held several meetings with the SVCDC, the residents, and the City of Houston; however, the project was stalled until SVCDC could provide acceptable plans and specifications.

SVCDC fought with residents.

Sometime between November 1999 and April 2000, one of the residents filed suit against the management alleging that the Board of Directors was improper and asking for a new election. The resident also requested that the renovations not take place until after the trial which was scheduled for August 21, 2000. In an additional lawsuit, three of the residents filed suit against the SVCDC and its Board of Directors seeking to prevent the Board from evicting the complainants. The initial suit was apparently successful because SVCDC seated a new Board of Directors in January 2002.

SVCDC fought with contractors.

After the original management agent/developer resigned in November 2001, SVCDC hired a new management agent/developer (Barron Builders) based on a recommendation from the Houston Multifamily office. However, SVCDC was dissatisfied with Barron Builders' assessment of how many repairs were necessary to complete renovations of the apartments. SVCDC requested the Fort Worth Multifamily Office to allow it to hire a different architect. Also, in November 2002, SVCDC took all bill payment responsibilities away from Barron Builders, leaving the management agent with only rent-collecting and bookkeeping duties. SVCDC claimed they took this action to make bill payments more timely. This action indicated that SVCDC was unhappy with the management agent's performance.

SVCDC failed to complete Phase I renovations properly.

The General Contractor (Roca) began first phase renovations on or about August 23, 2000, and claimed to have substantially completed them by January 26, 2001. The Multifamily Office and the OIG physically inspected the renovated apartments and determined that they did not meet HUD standards.

In November 2001, the Carver Institute severed its management agent/developer contract with SVCDC. SVCDC then elected a new Board of Directors with the complainant as the Chairman.

SVCDC implemented inappropriate compensation for its Board of Directors.

The Board of Directors voted to give the Chairman and Vice-Chairman rent-free apartments and to give each of the ten board members $300 a month for their services. Sometime between October 2002 and April 2003, two nonprofit organizations - the Texas Tenants Union and the

Local Initiatives Support Corporation, convinced SVCDC to stop the free rent and payments because they were inappropriate compensation for a nonprofit organization.

Compliance review of SVCDC operations.

In May 2001, the Multifamily Houston Office conducted a compliance review of SVCDC operations in four operational areas: general management; financial management; physical condition; and resident training and participation in SVCDC operations.

The compliance review outlined 23 problems that the Multifamily Office personnel found in all 4 operations areas. Some of the problems in each operational area were significant.

Significant problems in the general management area included: lack of critical documents such as leases and tenant income verifications; lack of documentation showing management's collections of security deposits, rents and fees from tenants; and illegal rent increases.

Significant problems in the financial management area included: lack of audited financial statements; inaccurate monthly financial reports; inability to reconcile the number of bank accounts maintained by the management agent; operating deficits of $489,000 for 1998 through 2000 and failure to repay the HOME loan; failure to escrow $30,000 per year in a reserve for replacement account as required by the contract for sale; and inability to provide a record of property assets.

Significant problems in the physical condition area included: failure to provide approved plans and specifications for the renovations; and 68 percent (19 of 28) renovated units failed to meet HUD standards while 59 percent (58 of 98) of non-renovated units failed to meet HUD standards.

Significant problems in the resident training and participation area included: the Computer Learning Center was underutilized; SVCDC did not implement the Resident Initiatives Development Plan to train residents to manage the apartment complex; and the SVCDC Board of Directors might not have represented the residents.

The Fort Worth Multifamily office attempted to regain control of the project.

Since SVCDC had not submitted approvable plans and specifications for the renovations, the Fort Worth Multifamily office suspended relocation payments in approximately December 1998. In March 1999, the Fort Worth Multifamily office complained to SVCDC that the SVCDC development team "had not been able to get to a point where the actual work on the project can begin" 6 months after the project rehabilitation was to have been completed. The Multifamily office blamed the problems on SVCDC's lack of organization and leadership. The complaint also stated that the Spanish Village residents were not being represented by the SVCDC board and stated that HUD would not discuss further actions or expenditures of grant funds until a new SVCDC Board of Directors had been elected and had reviewed the existing development team contracts. In a July 1999 memorandum, the Fort Worth Multifamily Office reiterated these complaints.

The Fort Worth Multifamily Office remained concerned about the lack of progress on the renovations and suspended all draws from the Upfront Grant between approximately January 1999 and May 2000. Later, in May 2001, after SVCDC had failed to complete Phase I renovations properly, the Fort Worth Multifamily office again suspended all Upfront Grant draws. The City of Houston HCDD did not process any further draws from the HOME loan after October 2001.

The Director, Fort Worth Multifamily office, issued a default letter dated August 27, 1999, declaring default under the grant agreement because none of the renovations had been completed, despite the Upfront Grant Agreement requirement that all renovations be completed by September 30, 1998. The letter indicated that either the City may foreclose or enter as a mortgagee in possession to complete the repairs, or HUD may exercise the options or remedies afforded by the agreement. This includes canceling or limiting project activities or payments; reducing or recapturing funds; terminating the grant; or assigning the grant to a mortgagee.

However, HUD Headquarters did not want to take the project out of the control of the residents. Headquarters did not allow the foreclosure to proceed and instructed the Fort

Worth Multifamily office to "work some more" with the SVCDC to get the project completed.

After Headquarters instructed the Fort Worth Multifamily office to "work some more" with SVCDC, the Fort Worth office allowed SVCDC to proceed with Phase I of the renovations. The May 2001 Multifamily Compliance Review showed that SVCDC failed to perform the renovations properly.

Enforcement Center recommended terminating the Upfront Grant.

In September 2001, the Enforcement Center conducted a review to determine whether SVCDC had complied with the terms and conditions of the Special Warranty Deed and the Upfront Grant Agreement. The Enforcement Center determined that SVCDC had failed to: (1) keep proper books and records; (2) certify tenant incomes; (3) maintain rents at the appropriate level; (4) complete renovations by September 1998; (5) provide resident services and training; and (6) provide for democratic elections of officers and directors. The Enforcement Center recommended that HUD terminate the Upfront Grant. It also said that HUD had the option to default the project, retake title, and complete the repairs. However, the Headquarters Multifamily office decided that SVCDC should have another chance to complete the renovation project because the management agent had resigned, SVCDC had changed its Board of Directors through democratic elections, and SVCDC had expressed an interest in completing the renovations.

In June 2002, the Fort Worth Multifamily office requested SVCDC to provide a new development plan by September 24, 2002. SVCDC provided the new development plan on September 23, 2002. The Fort Worth Multifamily office evaluated the plan and on October 31, 2002, told SVCDC the plan was inadequate because it did not identify all needed repairs or justify all costs. The memorandum also expressed doubt about SVCDC's 5-year plan.

HCDD did not want to be involved in the SVCDC renovation project.

In November 2001, the HCDD Director told us her office had never wanted to be involved with the SVCDC project. The director stated the City would not foreclose on the property, did not want it, and would allow HUD to take it back. She indicated her office would follow HUD's lead and would allow SVCDC to proceed with renovations only if HUD allowed it.

The Fort Worth HUD Multifamily Director prefers to retake title and ensure the project's completion.

On January 22, 2003, we met with the Director Multi-family Housing Division and staff of Multi-family Property Disposition. The Director of Multi-family Property Disposition was not available. The Multifamily officials did not have a plan to ensure the project would be completed and doubted if it could be completed using only the remaining Upfront Grant and HOME loan funds. The Director of the Fort Worth Multifamily Division indicated he believed his best option is to default the project under the various agreements and retake title to the property. He indicated HUD should then either sell the property to someone who would complete the repairs or use the FHA insurance fund to complete the repairs and then sell it to some organization that would operate it as low-income housing.

Conclusion

SVCDC did not complete property renovations in accordance with its agreements with HUD. On March 12, 2003, the Fort Worth HUD Multifamily office declared a default under the Upfront Grant Agreement. In the default letter, HUD gave SVCDC the option to either sell the property to a nonprofit entity with the capacity and experience to complete the rehabilitation and assign the remaining grant funds to that entity within 60 days or deed the property back to HUD within 60 days. HUD specified that if SVCDC sells the property above its cost, all profit must be returned to HUD as required by the Special Warranty Deed. We believe HUD should continue to exercise these remedies as provided by the various controlling documents. Also, if SVCDC does not comply with the instructions contained in the March 12 default letter, HUD needs to establish a plan of action and time frames to ensure the property's acquisition and completion of the renovations to bring the property up to acceptable standards.

Auditee Comments

SVCDC disagreed with our finding because it believed the current and former Boards of Directors are separate entities. The current SVCDC Board disclaimed any responsibility for the lack of progress on the renovations, and believes the audit was unfair because the auditors did not differentiate between the current and former Boards of Directors.

SVCDC did not dispute the amount of funds expended, although it did believe all of the Federal funds were expended improperly. The SVCDC also questioned the audit's lack of a finding of political influence.

We included SVCDC's full response in Appendix B.

OIG Evaluation of Auditee Comments

We believe the SVCDC is a single entity, regardless of who sits on the Board. Regarding Federal fund expenditures, we reviewed 100 percent of the Federal funds expended and found approximately $90,500 that were improperly expended out of $245,277 in HOME loan funds and no funds were improperly expended out of $788,735 in Upfront Grant funds. There were some unusual payments made, including prepayments to the Architect and the Developer. However, those payments were in accordance with contracts between SVCDC and its contractors, and all payments except the ones totaling $90,500 were proper and supported with documentation.

Regarding political influence, we reviewed a number of documents related to political influence and interviewed various levels of the Multifamily Division of HUD and found no "inappropriate influence."

Recommendations

We recommend the Director of Multifamily Housing Property Disposition continue with the remedial action he has started by:

1A. Establishing an acceptable plan of action with time frames to complete alternative measures to obtain and complete renovations to the property if SVCDC does not comply with HUD's options provided in the default letter of March 12, 2003, and,

1B. So that the funds can be put to better use, de-obligating the balance of the Upfront Grant to SVCDC, or, assigning the balance of the Upfront Grant ($1,477,710) to an acceptable owner who has the capacity to bring the property up to HUD Standards.

We also recommend that the Director of Community Planning and Development:

1C. If HUD terminates the project under SVCDC, ensure the City of Houston reimburses the City's HOME Investment Trust fund the amount expended on the project $245,228, including the $90,509 ($86,299 and $4,210) in ineligible and unsupported costs, and de-obligate the full amount of the obligated loan of $498,000 as HUD requires for projects terminated without completion, also,

1D. If HUD does not terminate the project; require the City to repay its HOME Investment Trust fund the $90,509 in ineligible and unsupported costs.

Management Controls

In planning and performing our audit, we obtained an understanding of the Spanish Village Community Development Corporation's and the HUD Multifamily Office management controls that were relevant to our audit. Management controls include the plan of organization, methods and procedures adopted by management to ensure that its goals are met. Management controls include the processes for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Management Controls.

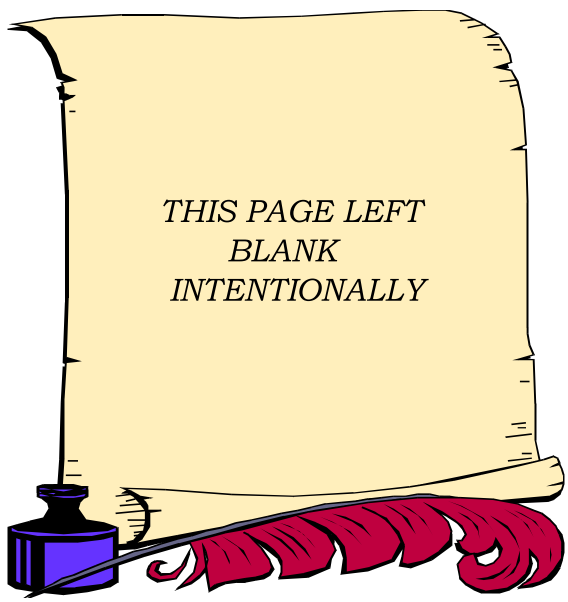
We determined the following management controls were relevant to our audit objectives:

- Controls over program policies and procedures;
- Controls to ensure the viability of projects, including assessing the capacity of key participants; and
- Controls over compliance with policies and procedures.

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.

We determined that none of SVCDC's management controls were reliable so did not rely on them. We covered specific Multifamily Office weaknesses in our findings and recommendations.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Schedule of Questioned Costs and Funds Put to Better Use

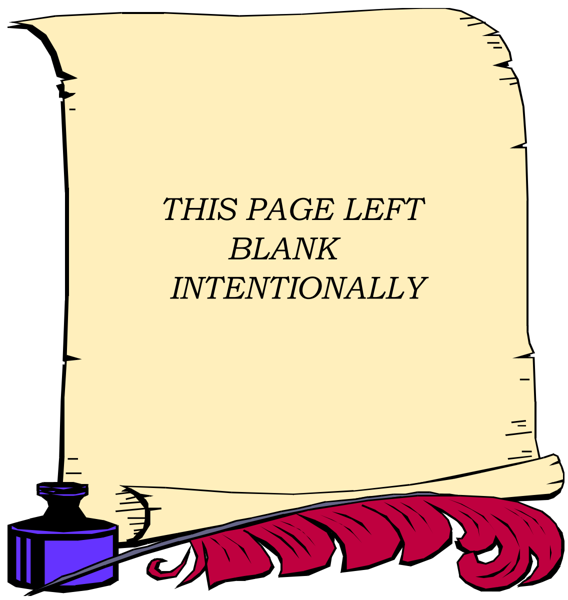
Finding and Recommendation	Type of Questioned Cost		
	Ineligible[1]	Unsupported[2]	Funds Put to Better Use[3]
1B			$1,477,710
1C			498,000[4]
1D	$86,299	$4,210	
Totals	**$86,299**	**$4,210**	**$1,975,710**

1 Ineligible costs are costs charged to a HUD-financed or HUD-insured 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 or HUD-insured 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.

3 Funds Put to Better Use are costs that will not be expended in the future if our recommendations are implemented. Funds Put to Better Use include: Costs not incurred; de-obligation of funds; Withdrawal of Interest subsidy costs on loans or loan guarantees, insurance or bonds; Reductions in Outlays; Avoidance of Unnecessary Expenditures; Loans and Guarantees not Made; and Other Savings.

4 Includes the ineligible and unsupported costs in recommendation 1E.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Auditee Comments

SPANISH VILLAGE COMMUNITY DEVELOPMENT CORPORATION, INC.
"Dedicated to Empowering Individuals, Families and the Community"

4000 Griggs Road – Suite 73 – Houston, Texas 77021 TEL. (713) 741-1936 FAX NO. (713) 741-3019

March 26, 2003

Mr. D. Michael Beard
Regional Inspector General for Audit
819 Taylor Street, Room 13A09
Fort Worth, Texas 76102

Re: Audit Report Draft Dated March 21, 2003

Dear Mr. Beard,

Response to this draft is very difficult because, in our opinion, the structure of the proposed report is seriously flawed. While this document responds to that draft, we believe that the difficulties presented by the draft should at least be noted:

1. The report should have been divided into two distinct sections:

    Section 1 should have dealt with the illegally constituted Spanish Village Community Development Corporation, which HUD, aware of its illegality, allowed to stay in control of the property until 2002.

    Section 2 should have dealt with the legally, democratically elected board that took power in 2002 and only months later was able to wrestle control of all pertinent, available records, bank accounts and other materials a few months later.

2. No description was given of attempts to verify political influence or involvement. While this aspect does not speak to present problems, it does deserve to be explored.

Methodology

While some of the first pages in the report are numbered, most are not. In order to respond, we have assigned page numbers to the report, numbering the title sheet ("AUDIT REPORT") page 1 and continuing through page 28.

(Page break)

Page 8 (Headed "Introduction"): Most of the allegations in this entire document refer to decisions unilaterally made by Dr. Alvin I. Thomas, and affirmed by individuals purporting to be officers of the Spanish Village Community Development Corporation. In fact, HUD ascertained and your report confirms that the SVCDC was not legally constituted. No legally constituted board existed before elections in January 2002. No effort was made by HUD to verify the legality of the entity with which it was dealing. Your report also acknowledge that the Houston HUD Office headed by former Housing Chief, Albert Cason and Larry Campbell formed a development team to implement the renovation and selected the Carver Institute (headed by Dr. Alvin Thomas) to be the lead member of the team.

That acknowledgment alone proves that HUD is the reason that this project has failed and not the SVCDC, because the SVCDC did not have any control over the project. Your report further states that "the SVCDC had previously hired Dr. Alvin Thomas as the Management Agent for the SVCDC". The SVCDC did not know anything about Dr. Alvin Thomas until Larry Campbell met with the purported board in 1995 and recommended that they hire Dr. Alvin Thomas as the developer (Not the Management Agent).

Paragraph 3 of that page fails to mention that Spanish Village was included in properties available for resident ownership under HUD's HOPE II Program. Dr. Alvin Thomas was given sole rights to train and organize the residents in advance of the property being deeded and was given a substantial grant to perform those tasks. In fact, he failed to perform in accordance with his grant proposal. This should have been part of the subject audit, and we want it included in the audit.

By lumping activities and shortcomings that occurred prior to January 2002 (When we took office), including those even prior to 1996, with those since that date, the Office of the Inspector General is, in our estimation, blaming the present membership and board for;

1. Activities by an illegally constituted body, and

2. Failure by the contractor (Dr. Alvin Thomas) who controlled Spanish Village until January 2002 to provide training for which he was contractually obligated.

Page 9 (page beginning "Maintaining projects..."): As mentioned earlier, we find no description of any interview or investigation concerning political influence or involvement, while most of the correspondence from Dr. Alvin Thomas and SVCDC that was provided to you suggest otherwise.

You indicated that your field audit was conducted between May 2001 and March 2003. No differentiation is made between the period when the property was under the control of Dr. Alvin Thomas and afterward. In fact, most of the allegations of improprieties relate to the period during which Dr. Alvin Thomas was in control, because the legally constituted board never had access to <u>any</u> of the federal funds.

Page 11 (page headed "Spanish Village Community Development Corporation Defaulted..."): By your own admission, your audit was prompted by a citizen complaint. Specifically, that complaint was mine. I was calling to your attention that nothing was being done about the default on the grants and loans and that, in fact, the SVCDC was not legally constituted at the time. Yet HUD continued to deal with that entity, in spite of questionable elections and the inability of the nominal President to respond intelligently, instead delegating all responses to Dr. Alvin Thomas.

You go on to state that the "SVCDC has not completed HUD funded renovations on the Spanish Village Apartments for more than four years after it was supposed to be completed".

As noted in your report on the page titled "Introduction", The Houston HUD Office headed by Albert Cason formed a development team to implement the renovation project and selected the Carver Institute (headed by Dr. Alvin Thomas) to be the lead member of the development team, yet you blame the SVCDC for failing to complete the project. What's wrong with this picture?

Page 13 (page starting "Office and an effective review..."): You stated that the SVCDC continuously demonstrated its inability to complete the project and list seven specifics. Again, all these problems occurred during Dr. Alvin Thomas's watch, when the SVCDC was not legally constituted.

Page 18 (page beginning "2001, after SVCDC had failed..."): You state: "...HUD Headquarters did not want to take the project out of the control of the residents." Unless you have specific documentation to that effect, you cannot state that as a fact. You might have written something like that to "Alvin Braggs, Multifamily Housing Director, in the Fort Worth HUD office, stating that HUD headquarters did not want to take the property out of the control of the residents." However, HUD was aware at the time that Spanish Village was not under the residents control, but under the control of Dr. Alvin Thomas , his attorneys and other professional resources.

Your draft report fails to recite that the SVCDC during the period when the SVCDC was being controlled by Dr. Alvin Thomas also signed a construction contract with ROCA Construction Company in 1999, shortly after HUD declared the SVCDC to be in default, and that contract was approved by HUD and the City of Houston Department Housing & Community Development, even though there were no approved plans and specifications on which the bids could have been taken. The Plans and specifications were not approved until 2000. No questions were raised about possible favoritism given to Roy Owens II, (President of ROCA Construction Company).

** (page break)**

Summary

HUD Headquarters, HUD Multifamily Housing PD, the Enforcement Center and now the HUD Inspector General, after cutting Dr. Alvin Thomas slack for more than six years, is now holding the present, and only legally-constituted board in the history of the SVCDC, responsible for all of Dr. Thomas's shortcomings. We have been unable to get the development plan approved due to the submission of the plan by Barron Builders (recommended by HUD) and Lee Huebel without the board's review or approval. The new board is operating in accordance with its Bylaws, and the stipends and two free apartments that were provided for two officers are no longer provided. These are the only problem areas cited by the Audit, but have nothing to do with the federal funds that HUD has wasted because the new board never had access to the funds.

Even though you hold HUD operations responsible for lack of oversight and enforcement, we feel that your report is clearly biased against the SVCDC, because as you acknowledged in your report that the Houston HUD Office, not the SVCDC formed a development team and is responsible for bringing Dr. Alvin Thomas to the SVCDC, yet, the SVCDC are the only ones being punished for the actions – or inaction's of HUD, the City Department of Housing & Community Development, Dr. Alvin Thomas and HUD's development team.

Your report includes statements that are clearly untrue. Case and point, on the page titled "Introduction", you claim that the SVCDC spent $788,734.50 of the Up-Front Grant between September 1996 and January 2003, while in actuality the funds were spent between 1996 and 2001, while Dr. Alvin Thomas and the illegal board was in control. Continuing to group the two boards together is not fair. The current board never had access to any of the Up-Front Grant or City Loan funds because they were frozen when we took office in January 2002 and continued to this date, yet the current board has made improvements on the property without the HUD funds.

Your report states that SVCDC did not plan the project well, SVCDC relocated tenants without HUD approval, SVCDC violated procurement rules and incurred $90,500 of ineligible and unsupported expenses from the HOME loan and SVCDC prepaid the architect and developer.

SVCDC never controlled anything, and for you to misrepresent the facts is simply wrong. HUD put the development team together and selected Dr. Alvin Thomas to run the show while hiding behind an illegal board. The Houston HUD office set this project up to fail from the start as noted in your report on the page titled "SVCDC continuously demonstrated its inability..." the Houston HUD Office understated the estimated cost on the original form 9552 by $271,613, Therefore the SVCDC was facing failure from day one because of HUD's actions. Also, for your report to claim that the SVCDC prepaid the architect and developer is unfair because all payments came from the Up-Front Grant and the City Loan and had to be approved by HUD and City Officials, therefore it should be noted in your report that HUD and City Officials prepaid the developer and the architect. In regards to relocating residents without HUD approval, the funds came from the Up-Front Grant therefore someone had to approve the request by Dr. Alvin I. Thomas to relocate the residents when no "Notice to Proceed" from HUD or the City HCDD was issued.

The recommendations from report endorse the action taken by HUD and clearly ignore the facts. Your recommendations also negate the years in which the residents of SVCDC have fought to gain control of our property, and we feel that we are being treated this way because we are poor and the bottom line is to take the property away from us.

Since you claim that the focus of the audit is on the Up-front Grant and City Loan, the SVCDC would like to know why your report does not recommend recovering the funds that were improperly paid to the members of HUD's development team? Because to this day, they have not fulfilled their contractual obligations, and after all, these funds came from the Up-front Grant and City Loan.

Given the fact that HUD formed the development team and brought in Dr. Alvin Thomas to work with a board that was never constituted, we feel that the SVCDC now has competent leadership to get the renovation underway and completed within a reasonable time frame. The new board has an architect ready to revise the development plan, pending HUD approval of course. The new board has a development team set up including management, an accountant and legal Counsel. All we need is a chance to show that we are capable of making this project work without recommendations from HUD, because every person that HUD has suggested we work with have failed us, yet the SVCDC is blamed for the failure.

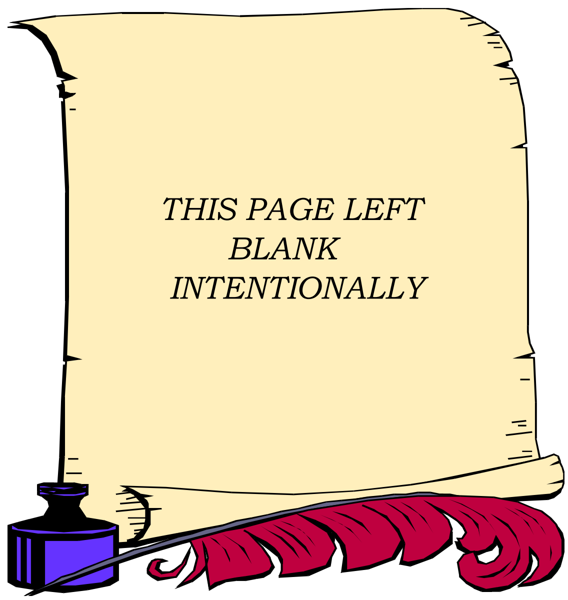
In closing, we are requesting that a copy of our response be distributed to every government agency listed on your Distribution Outside of HUD list and also include the SVCDC.

Sincerely,

Marvin Norman

Marvin Norman
President

Cc:
SVCDC Board of Directors
Congresswoman Sheila Jackson Lee
Congressman Tom Delay
Congressman Gene Green
Senator Kay Bailey Hutchison
Senator John Cornyn
Ada Edwards, Council Member
Michael Berry, Council Member
Carroll Robinson, Council Member
Annise Parker, Council Member
Gordon Quan, Council Member
Daisy Stiner, COH
Lee P. Brown, Mayor
Katie Worsham, HUD
Alvin Braggs, HUD
E. Ross Burton, HUD
Dr. John Weicher, HUD
Jerry Thompson, HUD OIG
David Turner, HUD EC
Samuel Keeper, TACH
Deloyd Parker Jr., SHAPE
Sylvester Anderson, Attorney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Spanish Village Community Development Corporation

Chairman, Committee on Government Affairs

Senior Advisor, Subcommittee on Criminal Justice, Drug Policy & Human Resources

House Committee on Financial Services

Senior Counsel, Committee on Financial Services

Committee on Financial Services

Managing Director, Financial Markets and Community Investments, U.S. GAO

Chief Housing Branch, Office of Management and Budget

Department of Veterans Affairs, Office of Inspector General

Chairman, Committee on Government Affairs
172 Russell Senate Office Building, Washington, D.C. 20510

Chairman, Committee on Government Reform
2348 Rayburn Building, House of Representatives, Washington, D.C. 20515-4611

Ranking Member, Committee on Government Reform
2204 Rayburn Building, House of Representatives, Washington, DC 20515