



U.S. Department of Housing and Urban Development
Region 6, Office of Inspector General
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July 2, 2003

2003-FW-1805

MEMORANDUM FOR: Frank Padilla
Director
Office of Community Planning and Development, 6BD

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

SUBJECT: Citizen Complaint
Housing Rehabilitation Program
Department of Family and Community Services
Albuquerque, New Mexico

INTRODUCTION

In response to a citizen complaint,¹ we reviewed the City of Albuquerque's (City) Housing Rehabilitation Program (Program). The overall objective was to determine whether the City managed its Program in accordance with City and HUD requirements. Specific review objectives included determining whether the City: (1) selected, managed, and monitored projects in accordance with City and HUD requirements; (2) originated and serviced² loans in accordance with City and HUD requirements; and (3) selected contractors in accordance with procurement policies and procedures.

Overall, the City's Program complied with City and HUD requirements. However, the City could improve its management of the Program. Specifically, the City needs to strengthen its development of cost estimates including explicitly identifying the work required to rehabilitate a home. Further, the City should better advertise its Program. Additionally, the City should better document the information it provides to HUD.

We provided a discussion draft to the City on June 2, 2003. With acquiescence of the City, we had a conference call to discuss the draft on June 5, 2003. The City provided formal comments on June 17, 2003. The City was very responsive to the recommendations. We have included the

¹ In addition to the citizen complaint, Mayor Martin Chavez, City of Albuquerque; City Councilman Greg Payne; Senator Domenici; and Congresswoman Wilson requested we review the program.

² The City did not service the loans; AmeriNational Community Service Group serviced the loans. We did not review AmeriNational Community Service Group.

City's comments as an appendix. We considered the City's comments in preparing the final report.

We recommend HUD's CPD Director require the City to: (1) develop and implement cost estimation procedures for identifying the work and costs needed to rehabilitate a home; (2) revise and implement procedures regarding the creditworthiness of contractors; (3) develop and implement procedures approving demonstration programs; (4) develop and implement a comprehensive advertising program for its rehabilitation program; and (5) assure the accuracy of the information reported to HUD. In a May 30, 2003 discussion, the New Mexico CPD Director stated that he had reviewed the draft report and agreed with the recommendations.

In accordance with HUD Handbook 2006.06 REV-3, within 60 days please provide us, for each recommendation without a management decision, 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 review.

Should you or your staff have any questions, please contact William W. Nixon, Assistant Regional Inspector General, at 817-978-9309.

OBJECTIVES, SCOPE, AND METHODOLOGY

To accomplish our objectives, we interviewed City employees, contractors, and homeowners. We conducted onsite visits at properties rehabilitated with HUD funds. Further, we examined City records including annual reports to HUD, HUD system reports, loan files, and contractor files. We also examined selected contractor's records. Our scope included all project loans made from January 1, 2000, through October 18, 2002. Due to the inconsistency of the reports, we did not rely upon the accuracy of City's reports. We expanded the scope as necessary.

We selected 51 of the 153³ loans made between January 1, 2000, and October 18, 2002, for review. The 153 loans totaled \$5,785,660.⁴ We based the non-representative selection of loans on a weighted average of awards by contractor with the selection of at least one contract for each contractor and City loan officer. We statistically selected homeowners who received loans from the City during the review period to query their opinion of the Program. We also statistically selected homeowners who applied but did not receive loans.

³ 33 percent.

⁴ Average loan amount about \$37,800.

BACKGROUND

The City of Albuquerque (City), New Mexico, was founded in 1706, chartered as a town in 1885, and organized under territorial law as a city in 1891. The City became a charter city in 1917, and the voters approved a home rule amendment to the charter in 1971. In 1974, the electorate voted to establish a mayor-council form of government; the City Council consists of nine council members.

The City's Program began in 1975 to benefit low-income households living in substandard conditions. The Program's goal "is to produce the best quality home rehabilitations while attempting to produce program income to ensure maximum future funding for rehabilitations of homes owned by low-income residents." The Program is "designed to provide decent housing, a suitable living environment, and expand economic opportunities to low and moderate-income individuals." Through the Albuquerque Housing Services, the City provides loans to applicants to rehabilitate their homes. Between January 1, 2000, and October 18, 2002, the City made 153 loans to homeowners.

In August 2001, the City's Internal Auditor issued a report on the Program. The findings indicated potential discrepancies between the way the City managed the Program and federal procurement guidelines at 24 CFR 85.36 and CPD Notice 91-01. The report also questioned the City's method for estimating rehabilitation costs. The report expressed concerns about the accuracy and review of cost estimates, inspection documentation, method used to select contractors, and documentation supporting contractor payment requests.

Both the Department of Family and Community Services and the City's Internal Audit Department requested that HUD review the City's rehabilitation loan program. HUD limited its review to an examination of the City's internal audit report. HUD concluded that the City conducted its homeowner rehabilitation program in compliance with federal guidelines and directives.

The City used HUD Community Development Block Grant (CDBG) and HUD HOME funds to finance their Program. The City's administrative building is located at 1840 University SE, Albuquerque, New Mexico.

Criteria

According to HUD requirements,⁵ CDBG and HOME funds may be used to finance the rehabilitation of any privately owned residential property, provided such rehabilitation meets a national objective of the CDBG Program.

According to CPD Notice 91-01,⁶ the City can assist the homeowner in retaining a contractor by providing a list of contractors, collecting and summarizing contractor bids, advising the owner on how to evaluate contractor proposals, and providing information on the past work of specific

⁵ CDBG requirements can be located in 24 CFR 570 and HOME requirements are located in 24 CFR 92.

⁶ Although expired, HUD staff state that it is still applicable.

contractors. In addition, the City can provide basic contract documents, including work specification and applicable federal requirements. The homeowner must select the contractor.

RESULTS OF REVIEW

While some problems exist regarding program management, none of the activities included in the allegations violated federal requirements.

The complainants alleged the City: (1) discriminated against some contractors and gave some contractors preferential treatment; (2) increased rehabilitation costs by requiring brand name materials and systems; (3) created the potential for fraud when it did not require formal competition; (4) used the program as a costly new home construction program; and (5) negligently approved waiver requests to increase loan ceilings and permit City employees to receive loans. Based upon our review, we did not find any evidence to support these allegations.

Additionally, the complainants alleged the City: (1) performed all of the duties necessary for awarding rehabilitation contracts except selecting the contractor and signing the contract; (2) counted non-immediate family members and non-relatives as permanent residents; and (3) rewarded qualified homeowners who violated City occupancy requirements by constructing new and larger replacement homes. Our work confirmed the validity of these allegations. However, HUD regulations permit the City to do it.

The City could improve its management of the Program.

Although the City complied with requirements, the City should improve its administration and delivery of the Program. Among other things, the City did not sufficiently identify the basis for its rehabilitation cost estimates. Further, the City improperly made three deferred loans, did not determine the creditworthiness of all contractors, and conducted a demonstration program without proper approval. In addition, the City should perform greater outreach to its residents.

Rehabilitation Cost Estimates and Work Specifications

Based on our review of 51 loan files, it appeared initially the City estimated its rehabilitation cost on the homeowner's available equity or maximum loan amount, and not the amount of labor and materials needed. The City determined estimated rehabilitation costs using the appraised value of the property after rehabilitation as a starting point. The City subtracted refinancing costs to determine available equity. If the available equity exceeded the maximum loan amount, the City usually used the maximum loan amount. Next, the City subtracted 5 percent for an emergency fund. The resulting total became the estimated loan amount. To determine the estimated rehabilitation cost, the City subtracted closing costs from the estimated loan amount. The City inspected the house and determined whether it could be brought up to code within the estimated rehabilitation cost. If it could, then it approved the project. If not, then the City disapproved the project.

Further, work specifications were not specific. The work required did not detail the labor and materials' costs to complete the project. For example for one project, the contractor was required to "construct a new furnace closet, complete with stand and a new 2050 hollow core door and jamb. Install ½" sheet rock in new closet. New closet to be constructed with 2" x 4" at 16" O.C. (centers) and deck for stand to be minimum of ¾" thick." The contractor said the cost to complete this task was \$300 while the inspector said \$350.

As another example, the contractor was required to install a front porch. The specifications stated:

"Install new 2"X4" frame then install new metal screen with trim to attach screen to 2"x4" frame. Install 3/8" masonite soffit at ceiling with h-molding, new ¾" decking over existing. Install new screen door lower half wood and upper half screen, Long Bell or preapproved equal. Paint all exposed wood trim, 2"x4"s and soffit. Contractor option of reusing existing deck at front and installing indoor/outdoor carpet."

The amount of materials and labor required was not identified. The City was able to operate in this manner because rehabilitation projects generally involved the same type of rehabilitation. Contractors had a general idea of the work required and could determine whether they could do it based on the City's cost estimate. If selected by the homeowner, this is how the contractor decided whether to accept the project.

The City should develop procedures to identify the labor and materials needed for the project and use it as their cost estimate. Further, work specifications should specifically identify what a contractor is expected to do to complete the project.

Improper Loans

In year 2000, the City violated its requirements by providing deferred loans to three homeowners whose anticipated annual income exceeded very low-income limits.⁷ Instead, the City should have made two loans at 6 percent and one at 3 percent. As a result, the City made \$117,067 in deferred loans to three homeowners who should have had to repay their loans with interest. This occurred because the loan officer did not include social security benefits in two cases and improperly calculated potential income in one case. We did not find this problem for loans made in years 2001 and 2002. However, the loan recipients were eligible for the Program and nothing in HUD's requirements prevents the City from providing deferred loans to these individuals. As a result, we are not recommending that the City repay its Program. Further, it did not appear that this occurred after 2000.

⁷ 50 percent of median income.

Creditworthiness

The City did not adequately determine the creditworthiness of some contractors. We reviewed files for 13 of 15 contractors identified as having participated in the Program. Of the 13 contractors, 10 were sole proprietorships and 3 were corporations. In addition to other verifications, the City verified the creditworthiness of contractors. For the 13 contractors, the City obtained credit reports based on the name of the applicant. Consequently, the City determined the creditworthiness of the sole proprietorships but not the corporations. Credit reports on individuals do not necessarily identify the financial stability of corporations. The City should revise its procedures to obtain credit reports on the corporation not the applicant.

Demonstration Program

For three loans we reviewed, the City specified the use of a specific roofing contractor. City officials said they specified the contractor as part of a demonstration program to determine whether this roofing method was superior to another method used. According to staff, they were trying to eliminate eventual leaks in the roofs. However, neither management nor the City Council approved the demonstration program. Such actions create the appearance of favoritism and raise questions about management. The City should develop procedures for approving such demonstration programs.

The City did not provide all qualified citizens with information about the Program

The City should perform greater outreach to its residents to ensure all eligible residents can participate. The program was supposed to be advertised using a brochure and the City's website. City officials acknowledged they did not issue the brochure to the public. Further, at the time of our review, information on the website was dated. For instance, information on participant's income limits was 2 years old. The City did update the information after inquiry. Based on interviews with 15 homeowners, participants learn of the Program through word of mouth. Further, four of the homeowners learned of the Program from City employees with two of them related to a City employee. The City should develop and implement a comprehensive marketing program designed to effectively publicize the Program and allow all eligible City residents the opportunity to participate in the Program.

Reporting Program Information to HUD

The City could not satisfactorily identify its CDBG and HOME funds expended on the Program between January 1, 2000, and October 18, 2002. This occurred because the City included rehabilitation project costs with administrative costs in its HUD reports. Further, the City could not trace costs reported in its annual HUD reports to supporting documentation. This occurred because the City did not maintain documentation supporting the information it submitted to HUD. Because of the difficulty in obtaining accurate information on the amount of CDBG and HOME funds used and the number of projects funded, we could not rely upon information provided by the City. The City needs to ensure the accuracy of information reported to HUD.

Other Matters

During the review, two matters arose that the City needs to address: builders risk insurance and verification of non-income earning adult residents. The City authorized contractors to begin work on a rehabilitation project before assuring the contractor obtained builders risk insurance. Instead, in several instances, the City accepted a contractor's statement that it had applied for builders risk insurance. During the review, the contractor's insurance agent verified that the contractor obtained the insurance. To strengthen the program, we recommend the City verify that contractor's have builders risk insurance before authorizing contractors to start a rehabilitation project.

As stated previously, the City properly verified the income of loan applicants who claimed they had income. However, it did not verify whether adult residents had income when they claimed none. Currently, the City has no ability to verify questionable assertions by the residents. The City can further ensure only eligible homeowners receive assistance by requiring all adults living in the house allow the City to verify income and credit information. We recommend the City require all adult residents to authorize access to their credit records and the ability to verify potential income. As a related issue, we suggested the City strengthen its applicant certifications regarding disclosure of all requested information.

THE CITY'S COMMENTS AND EVALUATIONS

On June 17, 2003, the City sent a written response to the discussion draft. We have included the response in its entirety as Appendix A. The City's responses addressed the issues raised in this memorandum. We were pleased the City noted actions taken and look forward to the City making additional improvements to strengthen its Program.

RECOMMENDATIONS

We recommend that the CPD Director require the City to:

- 1A. Develop and implement cost estimation procedures for identifying the work and costs needed to rehabilitate a home.
- 1B. Revise and implement procedures regarding the creditworthiness of contractors.
- 1C. Develop and implement procedures approving demonstration programs.
- 1D. Develop and implement a comprehensive advertising program for its rehabilitation program.
- 1E. Assure the accuracy of the information reported to HUD.

- 1F. Verify contractors have builders risk insurance before authorizing contractors to start a rehabilitation project.
- 1G. Obtain authorization from all adult residents to allow the City to verify income and credit information.

APPENDIX A



City of Albuquerque

P.O. BOX 1293 ALBUQUERQUE, NEW MEXICO 87103

Department of Family and Community Services

Martin J. Chavez, Mayor

Valorie A. Vigil, Director

June 17, 2003

D. Michael Beard
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Region 6, Office of Inspector General
819 Taylor Street, Room 13A09
Fort Worth, Texas 76102

Subject: Citizen Complaint, Housing Rehabilitation Program, Department of Family and Community Services, Albuquerque, New Mexico

Dear Mr. Beard:

We have reviewed the findings and recommended corrective actions in the draft report of the above referenced audit. We have no disagreements with the report findings and have already or will take the following actions to address the recommendations cited in the report:

1A. Develop and implement cost estimation procedures for identifying the work and costs needed to rehabilitate a home.

Action: This recommendation mirrors an earlier recommendation made by the City's Office of Internal Audit and steps have already been taken to improve cost estimating procedures.

1B. Revise and implement procedures regarding the creditworthiness of contractors.

Action: The City has implemented this recommendation. We now obtain credit reports from corporations separate from the applicant in those cases in which the contractors are corporations rather than sole proprietorships.

1C. Develop and implement procedures approving demonstration projects.

Action: The Housing Rehabilitation Program may now only undertake demonstration projects with the written approval of the Department Director. Demonstration projects must be for a limited period after which they must be terminated or incorporated into adopted program standards.

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1D. Develop and implement a comprehensive advertising program for [the] rehabilitation program.

Action: This recommendation also mirrors an earlier recommendation by the City's Office of Internal Audit and has been implemented.

1E. Assure the accuracy of the information reported to HUD.

Action: The City has begun to separate costs for the Housing Rehabilitation program operations from the costs of rehabs themselves. Source documentation supporting costs will be maintained in a more readily accessible manner.

We appreciate the professionalism of the staff of the Region 6 Office of Inspector General in their conduct of this review and look forward to the final report. If you have any questions, or need additional information, please contact Michael Passi, Associate Director of the Department, at 505-768-2865.

Sincerely,

A handwritten signature in cursive script that reads "Valorie A. Vigil".

Valorie A. Vigil, Director

DISTRIBUTION

Mayor Martin Chavez, City of Albuquerque, New Mexico

Senator Pete V. Domenici

Senator Jeff Bingaman

Congresswoman Heather Wilson

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