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To: Charles H. Williams, Director, HUD's Office of Multifamily Housing Assistance Restructuring, HY

Roger E. Niesen

FROM: Roger E. Niesen, Regional Inspector General for Audit, 7AGA

SUBJECT: Congressionally Requested Audit of the Outreach and Training Assistance Grant awarded to Housing Comes First, St. Louis, Missouri, Grant Numbers FFOT98018MO and FFOT00022MO.

INTRODUCTION

We have completed an audit of Housing Comes First and have determined that Housing Comes First did not comply with HUD and Office of Management and Budget (OMB) requirements. Specifically, Housing Comes First did not establish and implement controls to ensure grant funds were used according to applicable regulations. In addition, Housing Comes First could not adequately support how it used \$336,108 in grant funds, did not use a reasonable method to allocate costs, did not follow regulations when drawing down grant funds from HUD, and engaged in lobbying activities that possibly violated Federal regulations. Our report contains one recommendation that HUD take appropriate administrative action against Housing Comes First and its management.

Section 1303 of the 2002 Defense Appropriation Act (Public Law 107-117) requires the HUD Office of Inspector General to audit all activities funded by Section 514 of the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA). The directive would include the Outreach and Training Assistance Grants (OTAG) and Intermediary Technical Assistance Grants (ITAG) administered by the Office of Multifamily Housing Assistance Restructuring (OMHAR). Consistent with the Congressional directive, we reviewed the eligibility of costs with particular emphasis on identifying ineligible lobbying activities.

In conducting the audit, we reviewed Housing Comes First's records and interviewed responsible staff when available. Our audit testing was severely limited by the lack of availability of Housing Comes First staff and records. During our fieldwork, Housing Comes First effectively ceased operations due to lack of funds, and released all staff. Therefore, staff was not always available for interviews or to locate records.

Our audit work was further limited because the grantee lacked complete and reliable financial records. Housing Comes First's computerized accounting records began on December 15, 1998 and ended on February 2, 2001, covering only about half of the audit period of October 1998 through mid-November 2002. We tested the reliability of those computerized records that did exist and were unable to validate 27 percent of the disbursement journal entries reviewed when comparing the entries to bank statements and canceled checks. Adding to these problems was the fact that the grantee could not provide six bank statements and the related canceled checks for the period October through December 1998 for both OTAG-related bank accounts. The grantee also could not provide canceled checks for two other bank statements during the audit period. Due to these severe limitations, we were not able to review, nor draw conclusions about, a significant portion of the grantee's disbursements.

Because of these problems, and our desire to issue a timely report, we tested only the largest and most suspicious disbursements we were able to identify. In performing our testing, we used the bank statements that were available from Housing Comes First's two OTAG-related bank accounts to select individual disbursements for review. We reviewed all disbursements, for which we could locate canceled checks, of \$1,000 or higher and in the even amount of \$500. For each of these disbursements, we attempted to verify that they were appropriate and allowable uses of OTAG grant funds.

We also reviewed the requirements in the MAHRA, the OTAG Notices of Funding Availability, an OTAG grant agreement, HUD's requirements for grant agreements for nonprofit entities, and Office of Management and Budget's guidance on the allowability of costs for nonprofit grantees.

The audit covered the period September 30, 1998 through November 19, 2002. We performed the fieldwork at Housing Comes First, 5300 Delmar Boulevard, St. Louis, Missouri from June through mid-November 2002. Except for the testing limitations described above, we conducted the audit in accordance with Generally Accepted Government Auditing Standards.

In accordance with HUD Handbook 2000.06 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 audit.

Should you or you staff have any questions, please contact me at (913) 551-5870.

SUMMARY

Housing Comes First did not comply with HUD and OMB requirements. This occurred because Housing Comes First did not maintain a staff with the experience and knowledge necessary to effectively manage the organization. As a result, HUD has no assurance that grant funds were used within program requirements.

Housing Comes First did not comply with HUD and OMB requirements because it:

- Did not establish and implement controls to ensure grant funds were used according to applicable regulations. The grantee did not have adequate policies and procedures or complete and reliable accounting records. The grantee also did not segregate executive and financial functions or perform monthly reconciliations of its bank accounts.
- Could not adequately support how it used \$336,108 in grant funds.
- Did not use a reasonable method to allocate common costs. The grantee informed us that costs are allocated based on a predetermined percentage rather than on actual use or benefit.
- Made payment requests to HUD based on budget amounts when HUD regulations required it to obtain funds on a reimbursement basis for actual costs incurred.
- Engaged in lobbying activities that possibly violated Federal regulations.

We concluded that HUD has no assurance that grant funds were used within program requirements, or that Housing Comes First would properly use future OTAG funds. Therefore, our report contains one recommendation that HUD take appropriate administrative action against Housing Comes First and its management.

BACKGROUND

The Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA) established the Office of Multifamily Housing Assistance Restructuring (OMHAR) within HUD. Utilizing the authority and guidelines under MAHRA, OMHAR's responsibility included the administration of the Mark-to-Market Program, which included the awarding, and oversight of the Section 514 Outreach and Training Assistance and Intermediary Technical Assistance Grants. The objective of the Mark-to-Market Program was to reduce rents to market levels and restructure existing debt to levels supportable by these reduced rents for thousands of privately owned multifamily properties with federally insured mortgages and rent subsidies. OMHAR worked with property owners, Participating Administrative Entities, tenants, lenders, and others to further the objectives of MAHRA.

Congress recognized, in Section 514 of MAHRA, that tenants of the project, residents of the neighborhood, the local government, and other parties would be affected by the Mark-to-Market Program. Accordingly, Section 514 of MAHRA authorized the Secretary to provide up to \$10 million annually (\$40 million total) for resident participation, for the period 1998 through 2001. The Secretary authorized \$40 million, and HUD staff awarded about \$26.6 million to 38 grantees (for 81 grants awarded). Section 514 of MAHRA required that the Secretary establish procedures to provide an opportunity for tenants of the project and other affected parties to participate effectively and on a timely basis in the restructuring process established by MAHRA. Section 514 required the procedures to take into account the need to provide tenants of the project and other affected parties timely notice of proposed restructuring actions and appropriate access to relevant information about restructuring activities. Eligible projects are generally defined as HUD insured or held multifamily projects receiving project based rental assistance. Congress specifically prohibited using Section 514 grant funds for lobbying members of Congress.

HUD issued a Notice of Funding Availability in fiscal year 1998 and a second in fiscal year 2000 to provide opportunities for nonprofit organizations to participate in the Section 514 programs. HUD provided two types of grants. The Intermediary Technical Assistance Grant (ITAG) and the Outreach and Training Assistance Grants (OTAG). The Notice of Funding Availability for the ITAG states that the program provides technical assistance grants through Intermediaries to sub-recipients consisting of: (1) resident groups or tenant affiliated community-based nonprofit organizations in properties that are eligible under the Mark-to-Market program to help tenants participate meaningfully in the Mark-to-Market process, and have input into and set priorities for project repairs; or (2) public entities to carry out Mark-to-Market related activities for Mark-to-Market-eligible projects throughout its jurisdiction. The OTAG Notices of Funding Availability states that the purpose of the OTAG program is to provide technical assistance to tenants of eligible Mark-to-Market properties so that the tenants can: (1) participate meaningfully in the Mark-to-Market program, and (2) affect decisions about the future of their housing.

OMHAR also issued a December 3, 1999 memorandum authorizing the use of OTAG and ITAG funds to assist at-risk projects. OMHAR identified these as non-Mark-to-Market projects where the owners were opting out of the HUD assistance or prepaying the mortgages.

HUD's regulations at 24 CFR Part 84, contain the uniform administrative requirements for grants between HUD and nonprofit organizations. The regulation (24 CFR 84.27) requires that nonprofit grantees use the OMB Circular A-122, "Cost Principles for Non-Profit Organizations," in determining the allowability of costs incurred to the grant. OMB Circular A-122 outlines specific guidelines for allowability of charging salaries and related benefits to the grants and the records needed to support those salaries. For indirect costs charged to the grant, the Circular establishes restrictions for indirect costs, and specific methods and record keeping to support the allocation of costs.

OMB Circular A-122 also establishes the unallowability of costs associated with Federal and state lobbying activities. Simply stated, the use of Federal funds for any lobbying activity is unallowable. The Circular provides examples of unallowable activities regarded as lobbying. These include any attempt to influence an elected official or any Government official or employee (Direct Lobbying), or any attempt to influence the enactment or modification of any actual or pending legislation by propaganda, demonstrations, fundraising drives, letter writing, or urging members of the general public either for or against the legislation (Grassroots Lobbying).

Housing Comes First applied for OTAG grants in fiscal years 1998 and 2000. HUD awarded Housing Comes First OTAG grants of \$350,000 for 1998 and \$450,000 for 2000. The grantee spent the entire 1998 grant from October 1998 through April 2001, and all \$86,421 provided by HUD to date of the \$450,000 awarded under the 2000 grant. HUD has not provided funding to Housing Comes First since February 28, 2002; and according to the Executive Director, OMHAR has frozen funding for Housing Comes First.

In addition to the OTAG grant, Housing Comes First received funding from several other sources. These included the United Way of Greater St. Louis; Public Welfare Foundation; Local Catholic Campaign for Human Development - St. Louis Archdiocese; National Catholic Campaign for Human Development, the Butler Family Fund; St. Louis Resource Commission; Roblee Foundation; Missouri Housing Development Commission; and several individual donations.

Housing Comes First received a review of its financial statements for the fiscal year ended December 31, 2000. The results of the review demonstrated multiple, severe weaknesses in the grantee's internal controls.

FINDING 1

The Grantee Did Not Comply with HUD and OMB Requirements

Housing Comes First did not comply with HUD and OMB requirements. These problems occurred because Housing Comes First did not maintain a staff with the experience and knowledge necessary to effectively manage the organization. As a result, HUD has no assurance that grant funds were used within program requirements.

Housing Comes First did not comply with HUD and OMB requirements because it:

- Did not establish and implement controls to ensure grant funds were used according to applicable regulations. The grantee did not have adequate policies and procedures or complete and reliable computerized accounting records. The grantee also did not segregate executive and financial functions or perform monthly reconciliations of its bank accounts.
- Could not adequately support how it used \$336,108 in grant funds.
- Did not use a reasonable method to allocate common costs. The grantee informed us that costs are allocated based on a predetermined percentage rather than actual costs.
- Made payment requests to HUD based on budget amounts when HUD regulations required it to obtain funds on a reimbursement basis for actual costs incurred.
- Engaged in lobbying activities that possibly violated Federal regulations.

Inadequate Controls

Housing Comes First did not establish and implement controls to ensure grant funds were used and reported on according to applicable regulations. In particular:

- Policies and procedures were not adequate. The grantee did not have policies and procedures identifying how to account for grant funds and segregate costs among the various grants received. HUD regulation 24 CFR 84.21 requires that a grantees' financial management system provide for written procedures for determining the reasonableness, allocability and allowability of costs in accordance with the provisions of the applicable Federal cost principles and the terms and conditions of the award.
- Computerized data for disbursements was not complete or reliable. The grantee's computerized financial records covered only about half of the audit period, and we determined that 27 percent of the disbursements we selected from the grantee's bank statements during this period were not recorded in those records. In addition, the grantee ceased using the computerized financial database on February 2, 2001, and financial data, when recorded, was maintained in spreadsheets on the computer hard drive or on computer disks maintained by the Executive Director, outside the financial database. HUD regulation

24 CFR 84.21 requires that a grantees' financial management system provide for records that identify adequately the source and application of funds for federally-sponsored activities. These records must contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income and interest.

- Duties between the accounting and executive functions were not properly segregated. The Executive Director performed all functions and controlled all aspects of Housing Comes First's financial process. The Executive Director also approved employees' timesheets (including his own), received the checks from a payroll service, signed the checks, and distributed them to employees. HUD regulation 24 CFR 84.21 requires grantees to provide for effective control over and accountability for all funds, property and other assets. The grantees must adequately safeguard all such assets and assure they are used solely for authorized purposes.
- Bank reconciliations were not performed on a monthly basis. Because the grantee did not practice proper cash management, it incurred numerous insufficient funds charges and bank service fees. OMB Circular A-122, Attachment B, Paragraph 16, "Fines and Penalties," prohibits grantees from charging grants for fines and penalties resulting from violations of, or a failure of the organization to comply with Federal, State and local laws and regulations. HUD regulation 24 CFR 84.21 requires grantees to maintain effective control over and accountability for all funds.
- Quarterly reports to OMHAR were not prepared and submitted as required. The grantee was required to submit quarterly reports to OMHAR, beginning with the period ending December 31, 1998. As of the date of this report, the grantee should have submitted 16 quarterly reports. However, the grantee provided only four quarterly reports to OMHAR. HUD's Notices of Funding Availability require grantees to submit a quarterly performance report to OMHAR that lists the properties and number of tenants assisted by the OTAG activities performed that quarter.

Housing Comes First told us it is working to develop and implement more detailed internal control procedures. The grantee agreed that its accounting records were not updated and that it lacked proper segregation of duties between the executive and accounting functions of the organization, attributing the inadequate controls to its lack of staff.

Inadequate Documentation

Housing Comes First could not adequately support how it used \$336,108 in grant funds. The grantee provided adequate support for only \$26,643 of the \$362,751 we reviewed. For each of these disbursements, we attempted to verify that they were appropriate and allowable uses of OTAG grant funds.

OMB Circular A-110 Subpart C: Post-Award Requirements, Financial and Program Management, and 24 CFR 84 "Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations," Subpart C, Sections 84.21 state the recipient's financial management systems must provide records that identify adequately the source and application of funds for federally

sponsored activities. The system must also include accounting records that are supported by source documentation.

OMB Circular A-122, Attachment B, Paragraph 7.m.(1) and (2), "Support of Salaries and Wages," says charges to grants for salaries and wages will be based on documented payrolls approved by a responsible officials(s) of the organization. The distribution of salaries and wages to awards must be supported by personnel activity reports. Reports reflecting the distribution of activity of each employee must be maintained for all staff members whose compensation is charged, in whole or in part, directly to awards. Reports maintained by non-profit organizations must account for the total activity for which employees are compensated and which is required in fulfillment of their obligations to the organization.

Because the grantee's financial records were incomplete and unreliable, we used the bank statements that were available from Housing Comes First's two OTAG-related bank accounts to identify disbursements. We reviewed all disbursements, for which we could locate canceled checks, of \$1,000 or higher and in the even amount of \$500. In all, we reviewed 186 of these disbursements totaling \$362,751. After selecting a disbursement for review, we identified the payee on the canceled check or bank memo and attempted to locate support documentation. We considered a disbursement supported if we were able to locate an invoice or similar document supporting the amount disbursed. We did not consider check requests, canceled checks, or payroll registers without accompanying timesheets as adequate support.

We determined that of the \$362,751 in disbursements reviewed, Housing Comes First could not adequately support \$336,108 (over 92 percent) of the disbursements reviewed. The support provided for the remaining \$26,643 showed the expenses were for appropriate and allowable uses of grant funds. A majority of the unsupported disbursements were for payroll expenses for which the grantee could not provide timesheets to adequately support the expenses.

Payroll Disbursements

Payroll expenses accounted for \$230,523 of the \$362,751 reviewed. Housing Comes First used an outside payroll service at different times throughout the audit period, but processed its own payroll when not using the outside service. For those pay periods processed by the outside service, the grantee provided payroll registers; however, we did not consider these adequate support without accompanying timesheets. Housing Comes First provided only 75 timesheets for our audit period, and we obtained 26 additional timesheets from OMHAR that the grantee had submitted with activity reports. Therefore, we had only 101 timesheets to support bi-weekly payroll expenses for the four-year audit period.

Non-payroll Disbursements

Non-payroll disbursements accounted for \$132,228 of the \$362,751 reviewed. Non-payroll disbursements consisted of travel, office equipment and supplies, printing and copying costs, mileage reimbursements, postage fees, training, telephone charges, and other similar expenses.

Housing Comes First attributed its deficient records to the lack of a bookkeeper. The grantee also told us that timesheets are maintained for all employees, but time spent on specific grants was not

consistently tracked. The grantee stated that it is setting up processes to ensure all timesheets detail the hours spent on each grant.

Unreasonable Cost Allocation Method

Housing Comes First did not use a reasonable method to allocate common costs, nor could the grantee show that HUD approved the cost allocation method used. OMB Circular A-122, Attachment A., Paragraph E. "Negotiation and Approval of Indirect Cost Rates," requires grantees which have not already established an indirect cost rate with a Federal agency to submit a cost proposal immediately after the organization is advised that an award will be made, and, in no event, later than three months after the effective date of the award.

The grantee informed us that costs are allocated based on a predetermined percentage rather than actual costs. The grantee derived the allocation percentage from the OTAG grant revenue as compared to the total revenue of the grantee. The grantee allocated 75 percent of all costs to the OTAG grants. However, the grantee could not provide documentation to support the method or to show how it resulted in a reasonable assignment of actual costs.

The grantee told us that although Housing Comes First does not have an approved allocation plan, the basis for the grantee's cost allocation is based on past experience and is conservative. The grantee acknowledged that HUD requires use of an approved plan and told us Housing Comes First will summarize its allocation plan and submit it to HUD for approval.

Improper Payment Requests for OTAG Funds

Housing Comes First made payment requests to HUD based on budget amounts when HUD regulations required it to obtain funds on a reimbursement basis for actual costs incurred. In addition, Housing Comes First cannot support the costs reimbursed by any of its payment requests. HUD regulation 24 CFR 84.22 states that reimbursement is the preferred method of payment to grantees. HUD may provide cash on a working capital advance basis, but is to only advance cash to the recipient to cover its estimated disbursement needs for an initial period generally geared to the grantee's disbursing cycle. Thereafter, HUD is to reimburse the recipient for its actual cash disbursements. When HUD determines a cash advance is warranted, grantees must maintain or demonstrate the willingness to maintain financial management systems that meet the standards for fund control and accountability as established in 24 CFR 84.21. However, as reported above, we determined that Housing Comes First did not have a financial management system that met the standards for fund control and accountability.

Housing Comes First used its budgeted costs to request payments from HUD rather than actual costs incurred. The grantee used the same budgeted amount of \$9,722 for 9 of 19 payment requests for the 1998 grant instead of requesting reimbursement for actual costs incurred. Because of inadequate records, we could not determine whether adjustments were made to correct any differences between budgeted and actual costs. HUD issued payments to Housing Comes First on 23 payment requests for the 1998 and 2000 grants. The grantee did not provide us with any support for the expenses listed in these 23 payment requests. The Executive Director told us he could provide support for the payment requests he submitted, but could not provide support for the requests of the prior Executive Directors. As of the date of this report we had not received support for any of the payment requests.

Housing Comes First told us that budgeted costs were used to request reimbursements in the early stages by the former Executive Directors. The grantee also said that upon engaging an accountant, it will attempt to reconstruct records so that an adjustment can be made and forwarded to OMHAR.

Improper Lobbying Activities

Housing Comes First engaged in lobbying activities that possibly violated Federal regulations. MAHRA specifically prohibited the use of Section 514 funds to lobby members of Congress. OMB Circular A-122, Attachment B, Paragraph 25, "Lobbying" also prohibits the use of grant funds to:

- Attempt to influence any Federal or State legislation through communication with any member or employee of the Congress or State legislature or with any government official or employee in connection with a decision to sign or veto enrolled legislation (Direct lobbying).
- Attempt to influence any Federal or State legislation through an effort to affect the opinions of the general public or any segment thereof. This includes the introduction of Federal or State legislation; or the enactment or modification of any pending Federal or State legislation by preparing, distributing or using publicity or propaganda, or by urging members of the general public, or any segment thereof to contribute to or participate in any mass demonstration, march, rally, fundraising drive, lobbying campaign, or letter writing or telephone campaign (Grassroots lobbying).

Our review of the Board of Directors' meeting minutes, Project Director reports, and tenant files identified the following references to lobbying:

- July 1999 Board of Directors' meeting minutes: "The lobbying in D.C. was fairly successful, but we need to shift our target priorities of Section 8 Buildings to those that not only have contracts expiring soon, but also buildings that are located in key Congressional districts so that we have more leverage with elected officials." The minutes also reflected: "Tenant Lobby trips on key issues to Jefferson City and Washington, D.C."
- May 2000 Project Director's report: "The other major project I undertook was lobbying for the passage of HB 1496 and SB 650 that tenants had lobbied for at the 5th Anniversary Conference."
- July 2000 Project Director's report: "Last year Housing Comes First conducted forums on renters rights, how to organize a building, federal and local housing policies, lobbying, tenant buyouts and foreclosures, and an affordable housing fund for St. Louis."
- Two of 24 tenant files we reviewed contained references to lobbying. One file contained statements regarding lobbying and lobbying trips in connection with the tenant association meeting for February and March 2001. The second file contained a letter to Congressional members urging support for pending legislation, specifically SB 1365 and SB 1248.

The grantee does not believe it used OTAG grant funds for lobbying activities, but used other sources of revenue for its lobbying efforts. The grantee also told us the HUD Office of Inspector General may have a broader definition of lobbying than Housing Comes First.

We recognize that Housing Comes First received non-Federal funds and may not have been restricted from using these non-Federal funds for lobbying activities. However, the grantee's records were inadequate to demonstrate whether non-Federal funds were used in the instances of lobbying identified.

We believe all these problems occurred because Housing Comes First did not maintain a staff with the experience and knowledge necessary to effectively manage an organization required to operate within Federal regulations. During the four-year period Housing Comes First conducted OTAG-related activities, the grantee had four Executive Directors, three Office Managers (bookkeepers), and five InfoLine Directors. Further, in a Management Letter issued to Housing Comes First regarding the review of its financial statements for fiscal year ended December 31, 2000, the CPA conducting the review reported extensive, severe internal control problems and stated that staff did not have a clear understanding of accounting policies and procedures. Housing Comes First has yet to correct the deficiencies cited in that report.

As a result of the problems described in this finding, HUD has no assurance that grant funds were used within program requirements, or that Housing Comes First would properly use OTAG funds in the future. To date, HUD has issued \$436,421 in payments to Housing Comes First under the 1998 and 2000 OTAG grants and \$363,579 has yet to be disbursed on the 2000 grant.

Section 1303 of the 2000 Defense Appropriations Act (Public Law 107-117) authorizes HUD to recapture OTAG funds and prohibit further HUD funds to grantees if the use of the OTAG funding did not meet the requirements of Section 514. Section 1303 says that to the extent the HUD Inspector General determines that the use of any funding for technical assistance does not meet the requirements of Section 514, the Secretary of HUD shall recapture any such funds. It further provides that no funds appropriated under Title II of Public Law 107-73 and subsequent appropriations acts for HUD shall be made available for four years to any entity (or any subsequent entity comprised of significantly the same officers) that has been identified as having violated the requirements of Section 514 by the HUD Inspector General.

We do not believe Housing Comes First has demonstrated adequate control over OTAG funds or adherence to program requirements as required by Section 514. Therefore, HUD should take all appropriate administrative actions against Housing Comes First and its management.

AUDITEE COMMENTS AND OIG EVALUATION OF AUDITEE COMMENTS

Excerpts from Housing Comes First's comments on our draft finding follow. Appendix B contains the complete text of the comments except for the enclosures that are not required for understanding.

Auditee Comments - General

Housing Comes First believes it has carried out the objectives for both of the Outreach and Training Assistance Grants it has received. Housing Comes First says that as a result of a second long-term

freeze in funds, they had to lay off the entire staff (including the current executive director, contrary to a statement in the draft report) and have been unable to engage an accountant to help improve/upgrade their financial management systems. Problems with getting timely payment of invoices from OMHAR have made it extremely difficult to maintain administrative staff, and has contributed to the high turnover rate for all other staff.

While the current Executive Director stated that he has made himself available at personal expense to provide the auditors access to records, he has not been available full-time due to the freeze. He says that during the six-month audit period, seldom was it brought to his attention that the auditors were unable to locate certain records, in such cases where they had been possibly misfiled or were indeed missing. In cases when problems were brought to his attention, efforts were made to provide/locate records. If given the opportunity, Housing Comes First says it is committed to upgrading its bookkeeping and accounting functions so that they provide the highest level of accountability.

Housing Comes First believes there have been inconsistencies throughout the audit process. Most importantly it is their opinion that the current funding freeze is very premature and not in accordance with normal HUD audit finding resolution procedures, as it was implemented based on an interim draft report that the Regional OIG provided to OMHAR. Housing Comes First believes that providing the draft to OMHAR was inappropriate, and the Regional OIG stated repeatedly (apparently not in good faith) that no draft report would be published to OMHAR or other parties until all audit fieldwork was completed and their comments included. Other inconsistencies included the many changes in the audit completion date, which made planning very difficult. It was Housing Comes First's initial understanding that the fieldwork was to have been completed by August 31, 2002. Instead, the final date ended up being November 22, 2002. Housing Comes First requested additional time to properly respond to the latest findings but was only granted one additional day.

Regarding staff qualifications, Housing Comes First believes that the denigrating statement that "...Housing Comes First did not maintain a staff with the experience and knowledge to effectively manage the organization..." is gratuitous and false. The Executive Director explained that current and past staff have a wide range of experience with community based and non-profit organizations, small business management, and military experience. He believes that problems were due in larger part to funding issues, inconsistent payments, low salaries, etc.

OIG Evaluation of Auditee Comments

Housing Comes First believes it carried out the objectives of the grants it received; however, it did not maintain appropriate records nor properly account for source and application of funds, an important requirement of the OTAG program. Although Housing Comes First believes it had an experienced staff, the condition of the files and records indicate the experience was not in the administrative and accounting areas.

We appreciate that the Executive Director provided us access to the audit site at his own personal expense. However, the Executive Director was informed on numerous occasions throughout the audit that we were not able to find supporting documentation. OIG originally planned to issue an interim report because the audit could not be completed on schedule due to difficulty in gaining access to records and sorting through unorganized files. OIG changed this plan and told Housing

Comes First that it would not issue the planned interim report. However, we did not state that we would withhold information from OMHAR until all fieldwork was completed and auditee comments received. As part of our normal audit process, we discuss draft findings with the appropriate HUD offices to ensure we have correctly assessed the situation before distributing findings to the auditee for comment. The delay in the ending date of the audit occurred because of difficulty in getting access to records and the poor organization of documentation.

Housing Comes First was informed of the extended audit time, and was provided the normal two-week period to submit its response to our draft report. We were only able to provide a one-day extension to that period due to constraints mandated by Congress.

Auditee Comments – Inadequate Controls

Housing Comes First agrees that their accounting records are behind due to administrative staffing cutbacks (loss of two bookkeepers). They attached financial management forms and a draft updated timesheet, which will better account for any lobbying activity.

Housing Comes First will draft an upgraded financial management plan, which will be implemented when the organization returns to normal operation.

Housing Comes First agrees that due to cutbacks, the Executive Director performed most of the accounting procedures. They do not agree that the Executive Director had sole access to cash, as their policy calls for three possible signatories: the Board President, Treasurer, and Executive Director. At least two of these officers must sign checks.

Housing Comes First explained that bank reconciliations are behind due to lack of staff.

While Housing Comes First understands that they should have submitted required quarterly reports, they said the reports were only requested (prior to submitting invoices for payment) beginning in 2001. Other delinquent reports will be completed when Housing Comes First can engage bookkeeping/accounting staff so that they can be assured that reports are accurate.

OIG Evaluation of Auditee Comments

Housing Comes First agrees with our conclusions that their records are not adequate or up-to-date and have planned some actions that should help correct the problem.

Although Housing Comes First acknowledges duties were not properly segregated, they do not agree that the Executive Director had sole access to cash since checks required two signatures. We acknowledge that Housing Comes First's policies require two signatures on checks; however, the Executive Director performed all functions and controlled all aspects of the financial process. We revised our finding to clarify this fact.

Regarding quarterly reports, the 1998 and 2000 OTAG Notices of Funding Availability say OTAG grantees must submit a quarterly performance report to the Director of the Office of Multifamily Housing and Restructuring.

Auditee Comments – Inadequate Documentation

Housing Comes First has located and attached an additional 107 timesheets that they believe were not seen or reviewed by the auditors. Also, after receiving this report, Housing Comes First counted timesheets in the files that the auditors apparently did review and counted 137 timesheets rather than 101. Housing Comes First believes this represents a discrepancy of 143 timesheets that may not have been reviewed by the auditors. Also, since receiving the report, Housing Comes First says it located additional non-payroll disbursement documentation. Housing Comes First believes this calls into question the accuracy of the finding, or at least, the dollar amounts of unsupported disbursements. Housing Comes First believes this likely occurred because documentation was misfiled and staff was not on hand at all times each day to ensure the auditors had all records.

Although the Executive Director stated that he was on hand to provide access to the files, he was not available at all times due to the funding freeze. He also stated he was not informed that the auditors had not located such a large number of timesheets in the file cabinets (as he assumed timesheets had not been misfiled). Housing Comes First realizes they should have had them properly filed, and when resources become available they plan to bring on staff to correct any other deficiencies.

Regarding activity reports, Housing Comes First stated that detailed narratives have been submitted to OMHAR accompanying invoices during the term of the current Executive Director, and during terms of previous staff (to the best of Housing Comes First's knowledge). Housing Comes First says regular, detailed activity reports are maintained by subordinate staff and submitted to the Executive Director, who incorporates the content into the narratives submitted to OMHAR and the Housing Comes First Board of Directors.

OIG Evaluation of Auditee Comments

Our review of disbursements considered only disbursements that equaled or exceeded \$1,000; therefore, it is possible the Housing Comes First was able to locate documentation for smaller disbursements that they believe we did not examine. Housing Comes First acknowledged that documents were misfiled. Numerous times during this review we informed Housing Comes First that we could not find supporting documentation and were told everything available was in the files where we were directed. Although we attempted to locate all necessary documentation, it is possible that we missed supporting documentation since there was no particular filing system. Documents were placed in drawers in no particular order. We believe our conclusions are accurate based on the condition of the records and the information made available to us during our review. We acknowledge that the total amount of unsupported costs could change during the audit resolution process if the auditee is able to establish a filing system and locate supporting documents.

Our report did not address activity reports prepared by Housing Comes First. We did, however, report that Housing Comes First did not submit quarterly reports to OMHAR as required by HUD's Notices of Funding Availability. We found that Housing Comes First submitted only 4 of 16 required quarterly reports.

Auditee Comments – Cost Allocation Method

Housing Comes First believes the cost allocation method it used during the past two years, although possibly flawed, is actually conservative since they have not been accounting for indirect costs

associated with the VISTA Volunteers and have spent more activity time than the percentage allocated.

It has been Housing Comes First's experience that the type and amount of information requested by OMHAR for invoice backup has been inconsistent, and OMHAR only recently asked Housing Comes First to submit a cost allocation plan (August 2002).

Housing Comes First would appreciate the opportunity to correct possible deficiencies in their allocation method.

OIG Evaluation of Auditee Comments

Housing Comes First did not provide any documentation to show that its cost allocation method resulted in a reasonable assignment of actual costs. We cannot conclude that the method Housing Comes First uses is reasonable until a realistic cost study is completed and documented. OMB Circular A-122 has required an approved cost allocation plan since the inception of the OTAG program.

Auditee Comments – Alleged Improper Lobbying

To the best of Housing Comes First's knowledge, they have not used any HUD or other public funds for lobbying. Housing Comes First says other funding sources were available to pay for that activity.

Housing Comes First also says lobbying, though a limited function of Housing Comes First's mission, was often carried out on overtime and volunteer hours not billed to any grant.

OIG Evaluation of Auditee Comments

We acknowledge that Housing Comes First had revenue sources other than Federal funds; however, Housing Comes First did not have adequate records to demonstrate that it did not use Federal funds for lobbying activities. As a result, HUD lacks assurance that Housing Comes First adhered to Federal Regulations. To more accurately report the situation, we changed the wording in our report to say "Housing Comes First engaged in lobbying activities, possibly violating Federal Regulations."

Auditee Comments – Recommendation 1A

Housing Comes First strenuously objects to the recommendation that funding be ceased and grant funds reprogrammed. They believe this is an extreme and overly harsh recommendation that would, if implemented, be detrimental to thousands of Missouri tenants that are experiencing the growing housing crisis.

Housing Comes First further urges that the freeze be lifted and they be reimbursed for the large amount of work that has already been carried out.

Housing Comes First said that it is and has been one of very few Missouri tenant-based and tenant-led organizations. Housing Comes First would appreciate the opportunity to correct and remedy deficiencies.

OIG Evaluation of Auditee Comments

Our recommendation is based on the conditions found and the information that was made available to us during the audit. The recommendation contains various options for the Director of the Office of Multifamily Housing and Restructuring. Additional information provided with these comments, as well as other information that may be provided during the audit resolution process, should be evaluated in reaching a final resolution.

RECOMMENDATION

We recommend that the Director of the Office of Multifamily Housing and Restructuring:

- 1A. Take appropriate administrative action against Housing Comes First and its management. HUD should consider actions such as ceasing funding, recapturing funds, requiring repayment, prohibiting future awards to the grantee, and imposing sanctions against Housing Comes First and its directors and management.

MANAGEMENT CONTROLS

In planning and performing our audit, we considered the management controls relevant to Housing Comes First's Section 514 program to determine our audit procedures, not to provide assurance on the controls. 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.

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

- Receipt of grant funds
- Disbursement of grant funds
- Allocation of common costs
- Financial recording and reporting of grant funds
- Selection and award of consulting and other service contracts
- Administrative (HUD) reporting of grant uses and results

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.

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

Housing Comes First does not have:

- Adequate support for grant expenditures (see Finding 1).
- Policies and procedures to ensure that time records met OMB Circulars A-110 and A-122 requirements (see Finding 1).
- A supported cost allocation plan to charge shared costs (see Finding 1).
- Policies and procedures to ensure lobbying activities are not directly or indirectly funded by Federal sources (see Finding 1).

FOLLOW-UP ON PRIOR AUDITS

The Office of Inspector General has performed no previous audit of Housing Comes First.

SCHEDULE OF QUESTIONED COSTS AND FUNDS PUT TO BETTER USE

| <u>Recommendation Number</u> | <u>Type of Questioned Cost</u> | | <u>Funds Put to Better Use 3/</u> |
|----------------------------------|--------------------------------|-----------------------|---------------------------------------|
| | <u>Ineligible 1/</u> | <u>Unsupported 2/</u> | |
| 1A | | \$336,108 | \$363,579 |

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 can include:

- Reductions in outlays – An implemented OIG recommendation that causes HUD not to issue Federal funds earmarked for a specific purpose to the audited entity. These funds would only be reprogrammable by HUD.
- De-obligation of funds from programs or operation – An implemented OIG recommendation which specifically addressed the need to de-obligate funds.

AUDITEE COMMENTS

Housing Comes First

December 5, 2002

Mr. Roger Niesen
 U.S. Department of Housing and Urban Development
 Great Plains Office of Inspector General for Audit
 Gateway Tower II -5th Floor
 400 State Avenue
 Kansas City, Kansas 66101-2406

For Information
 Call Scott Mills
 (314) 435-2361 or
 David Lander
 (314) 552-6000

VIA FACSIMILE, MAIL, 2nd PARTY DELIVERY

**AUDITEE (Housing Comes First) INTRODUCTION/ SUMMARY OF COMMENTS
 on Audit Case Number KC-02-0010**

We believe that Housing Comes First (HCF) has thus far carried out the objectives of both of the Outreach and Training Assistance Grants which it has received. We have done so with a relatively small yet very capable and qualified staff and in the face of a rapidly growing housing crisis. Our work has been conducted while experiencing delayed grant payments and freezes 11 out of the last 23 months.

As a result of a second long-term freeze in funds, we have had to lay off the entire staff (*Including* the current executive director, contrary to a statement in the draft report) and have been unable to engage an accountant to help improve/upgrade our financial management systems. Problems with getting timely payment of invoices from OMHAR have made it extremely difficult to maintain administrative staff, and has contributed to the high turnover rate for all other staff. For the period of January 1, 2001 through August 15, 2002 (19 months) we have only received payment for OTAG activity conducted for nine of those months. The first freeze resulted in a four-month shutdown. The latest delayed payment has been (in our case) since August 2002 until the present. OMHAR was not only inconsistent with payments but also in what report information they requested along with invoices. For example, no cost allocation plan was requested until August 2002.

While the current Executive Director has made himself available at personal expense to provide the auditors access to records, he has not been available full-time due to the freeze. During the six-month audit period, seldom was it brought to his attention that the auditors were unable locate certain records, in such cases where they had been possibly mis-filed or were indeed missing. In cases when problems were brought to his attention, efforts were made to provide/locate records (such as certain bank statements that were ordered from the bank). We have consulted with two reputable accounting firms hoping that they could help correct existing deficiencies. One of the firms conducted our management review for the year 2000. Neither has been able to send in anyone as of yet for the necessary time needed nor can they work on a pro-bono basis. Neither of them wanted to work intensively in the office while OIG auditors were reviewing the same records. As a result of staff layoffs and the inability to pay for an accountant, significant backup/support records were not found. We were not aware until receiving this report that the auditors had only located such a small number of the timesheets from the files. Since receiving this draft report, we have located 107 additional timesheets. (OTAG related staff) we believe were not reviewed by the field auditors. More notably, after counting the time records that were apparently reviewed, we counted 137 for staff that worked on the OTAG program (in some capacity) rather than the reported 101 timesheets. This calls into question the accuracy of the finding. We have attached the additional timesheets located thus far that may not have been reviewed. Also enclosed is non-payroll disbursement material we think was not reviewed. We will also include bank statements that had to be ordered upon being informed by the auditors that they could not be located. When we have resources, we will be better able to hire staff and engage an accountant to reconcile other problems.

AUDITEE (Housing Comes First) COMMENT SUMMARY (Cont.)

2

If given the opportunity, HCF is committed to upgrading its bookkeeping and accounting functions so that they provide the highest level of accountability. A list of existing control procedures (such as the two check-signer policy the audit report failed to mention) was attached with the first set of interim comments and will be attached again.

We believe there have been inconsistencies throughout the audit process. Most importantly it is our opinion that the current funding freeze is very premature and not in accordance with normal HUD audit finding resolution procedures, as it was implemented based on an *interim draft report* that the Regional OIG provided to OMHAR. We believe that providing the draft to OMHAR was inappropriate, and the Regional OIG stated repeatedly (apparently not in good faith) that no draft report would be published to OMHAR or other parties until all audit fieldwork was completed and our comments included. Other inconsistencies included the many changes in the audit completion date, which made planning very difficult. It was our initial understanding that the fieldwork was to have been completed by August 31, 2002. Instead, the final date ended up being November 22, 2002. We requested additional time to properly respond to the latest findings but were only granted one additional day.

In the past, HCF has worked to concentrate its limited grant funds on the program objectives and not to spend an inordinate amount on administrative costs as is indicated by the dollar amounts (billed to administration) on the drawdown invoices. Unfortunately, administrative costs often are the first to be cut when operation is hampered by non-payment of invoices. Detailed activity reports accompanying the invoices (as well as material in the program files) indicate the large volume of work carried out over the four-year period. The many properties worked in were clearly program-eligible and efforts have resulted in many properties being saved from "opt-out" and others being "restructured". More recent examples (before having to cease OTAG operations) include helping save 160 units of affordable housing in St. Charles, MO (an area of very scarce affordability) and so far stopping demolition of 50 units in southeast Missouri (a rural area of high-poverty) and 12 units in St. Louis. In some cases we had to take drastic action such as civil suits (against government and private entities) in order to ensure that low-income people were not displaced.

Regarding staff qualifications, the denigrating statement that "...HCF did not maintain a staff with the experience and knowledge to effectively manage the organization..." is gratuitous and false. Current and past staff has a wide range of experience with community based and non-profit organizations, small business management, and military experience. Problems were due in larger part to funding issues, inconsistent payments, low salaries, etc.

Findings were also reported that HCF improperly lobbied. To the best of our knowledge, HCF did not use federal funds for any lobbying activity (as stated in the previous set of comments) and the OIG finding does not give a quantified dollar amount for the alleged violation. As was noted there are multiple other funding sources from which some lobbying expenditure was allowable. We believe that any lobbying activity was carried out well within amounts provided by these non-government sources. Often, such advocacy was conducted on volunteer time not billed to any grant. Lobbying, though one function of our mission comprises a very small percentage of our activity.

AUDITEE (Housing Comes First) COMMENT SUMMARY (Cont.) 3

We strenuously disagree with the recommendation that funding be ceased and or recapture of funds be implemented. This is not only overly harsh, but provides no opportunity for any remediation or corrective action. The thousands of Missouri tenants that are at risk of losing their homes will be the victims of such an action. The many tenants that we have already helped would surely also object. Even with the ongoing payment problems and other negative circumstances, the records reflect the tremendous amount of work carried out on these grants and the many accomplishments. Moreover, HCF has yet to receive reimbursement from HUD for large amounts of the work conducted under contract (nearly a full year's worth).

Below, we will more specifically address the findings broken down by four main categories: (1) Inadequate Controls (2) Inadequate Documentation (3) Cost Allocation Method (4) Alleged Improper Lobbying

Inadequate Controls—

We have attached a list of current control procedures along with our by-laws. We agree that our record our accounting records are behind due to administrative staffing cutbacks (loss of two bookkeepers). We have attached financial management forms and a draft updated timesheet, which will better account for any lobbying activity.

We will be drafting an upgraded financial management plan, which will be implemented when the organization returns to normal operation.

We agree that, again, due to cutbacks, the Executive Director performed most of the accounting procedures. We do not agree that the Executive Director had sole access to cash, as our policy calls for three possible signatories: the Board President, Treasurer, and Executive Director. At least two of these officers must sign checks.

Bank reconciliation's are behind due to lack of staff.

While we understand that we should have submitted quarterly reports and are required, they were only requested (prior to submitting invoices for payment) beginning in 2001. Other delinquent reports will be completed when we can engage bookkeeping/ accounting staff so that we can be assured that reports are accurate.

Inadequate Documentation ---

We have located and attached an additional 107 timesheets that we believe were not seen or reviewed by the auditors. Also, after receiving this report, we counted timesheets in the files that the auditors apparently did review and counted 137 timesheets rather 101. This represents a discrepancy of 143 timesheets that may not have been reviewed by the auditors. Also since receiving the report we have located and attached additional non-payroll disbursement documentation. This calls into question the accuracy of the finding, or least the dollar amounts of unsupported disbursements. This likely occurred because they were mis-filed and staff was not on hand at all times each day to ensure the auditors had all records. Although the Executive Director was on hand to provide access to the files, he was not available at all times due to the funding freeze. We were not informed that the auditors had not located such a large number of timesheets in the file cabinets (as it was assumed they had not been mis-filed). We realize we should have had them properly filed, and when resources become available we will be able bring on staff to correct any other deficiencies.

AUDITEE (Housing Comes First) COMMENTS (Cont.)

4

Regarding activity reports, detailed narratives have been submitted to OMHAR accompanying invoices during the term of the current Executive Director, and (as far as we know) during terms of previous staff. Regular, detailed activity reports are maintained by subordinate staff and submitted to the Executive Director, who incorporates the content into both the narratives submitted to OMHAR and in Executive Director's submitted regularly to the HCF Board of Directors.

Cost Allocation Method ---

We believe the cost allocation method HCF has used during the past two years, although possibly flawed, is actually conservative as we discovered that we have not been accounting for indirect costs associated with the VISTA Volunteers and have spent more activity time than the percentage allocated.

It has been our experience that the type and amount of information requested by OMHAR for invoice backup has been inconsistent, and we were only recently asked to submit a cost allocation plan (August 2002).

We would appreciate the opportunity to correct possible deficiencies in our allocation method.

Alleged Improper Lobbying

To the best of our knowledge, HCF has not used any Utilized any HUD or other public funds for lobbying. Other funding sources were available and applicable for this (very small) percentage of our overall activity.

Often, lobbying, though a limited function of our mission, was carried out on overtime and volunteer hours not billed to any grant.

AUDITEE (Housing Comes First) COMMENTS (Cont.)**5****Comments on Recommendation 1A---**

We strenuously object to the recommendation that funding be ceased and grant funds reprogrammed. This is an extreme and overly harsh recommendation that would, if implemented, be detrimental to thousands of Missouri tenants that are experiencing the growing housing crisis.


We further urge that the freeze be lifted and HCF be reimbursed for the large amount of work that has already been carried out.

HCF is and has been one of very few Missouri tenant-based and tenant- led organizations. The activity reports submitted to HUD and to the Board of Directors, along with the many media clips detail the efforts of HCF to ensure that low-income tenants have a voice and are given input concerning their homes and quality of life. We would appreciate the opportunity to correct and remedy any deficiencies so that this important work can continue.

Should you have more questions or require further comment please feel free to call either Scott Mills (314) 435-2361 or David Lander (314) 552-6000.

Sincerely,


Scott Mills,
Executive Director


Alicia Brown,
President

CC: Mr. David Lander, Thompson Coburn LLP

Enclosures:

Draft timesheet, expense forms, list of control procedures, by- laws,
check request form, deposit voucher additional bank statements,
additional timesheets for review, additional expense documentation

DISTRIBUTION OUTSIDE OF HUD

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The Honorable Joseph Lieberman, Chairman, Committee on Government Affairs, 706 Hart Senate Office Bldg., United States Senate, Washington, DC 20510

The Honorable Fred Thompson, Ranking Member, Committee on Governmental Affairs, 340 Dirksen Senate Office Bldg., United States Senate, Washington, DC 20510

The Honorable Dan Burton, Chairman, Committee on Government Reform, 2185 Rayburn Bldg., House of Representatives, Washington, DC 20515

The Honorable Henry A. Waxman, Ranking Member, Committee on Government Reform, 2204 Rayburn Bldg., House of Representatives, Washington, DC 20515

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