audit report

Issue Date
March 25, 2004
Audit Case Number
2004-PH-1005

TO: William D. Tamburrino, Baltimore Public Housing Program HUB, 3BPH

FROM: Daniel G. Temme, Regional Inspector General for Audit, Mid-Atlantic, 3AGA

SUBJECT: Petersburg Redevelopment and Housing Authority
Nonfederal Entities
Petersburg, Virginia

INTRODUCTION

We audited the Petersburg Redevelopment and Housing Authority's (Authority) interface with its three affiliated nonfederal entities. Our objective was to determine if the Authority improperly used U.S. Department of Housing and Urban Development (HUD) funds to develop and support these entities.

To accomplish our objective we reviewed applicable federal and HUD regulations, and the Authority's Annual Contributions Contract with HUD. We also interviewed appropriate Authority and HUD Program staff and reviewed other relevant documents including partnership agreements, financial statements, general ledgers, bank statements, bank loan agreements, related correspondence, and minutes from Board meetings.

We conducted the audit from July 2003 through December 2003. The audit covered the Authority's operations from January 2000 through December 2003. We expanded the scope of the audit as necessary and performed 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 and 120 days after report issuance for any recommendation without a management decision. Also, please furnish copies of any correspondence or directives issued because of the audit.

Should you or your staff have any questions please contact Mr. John Buck, Assistant Regional Inspector General for Audit, at (215) 656-3401, extension 3486.

SUMMARY

The Authority regularly used federal funds improperly to support its nonfederal entities and placed its Annual Contributions Contract assets at risk by improperly guaranteeing the debt of two of its three affiliated nonfederal entities. This occurred because the Authority did not properly account for work its employees performed, and failed to establish appropriate management controls to prevent it from encumbering or pledging its federal assets without HUD approval. The Authority's high management turnover, inadequate financial system, and practice of allowing key Authority personnel to serve in similar roles for its nonfederal entities contributed to these problems.

As a result, the Authority improperly pledged assets to guarantee debt incurred by its nonfederal entities estimated at $950,318. Additionally, the Authority paid salaries estimated at $620,236 from federal funds for work its employees performed in support of its affiliated nonfederal entities on a part-time basis from January 2001 until December 2003. Further, we estimated the Authority could more effectively utilize another $370,415 annually by ensuring it was properly accounting for and receiving reimbursement for work its employees performed for its affiliated nonfederal housing projects, and by preventing apparent conflict of interest situations in the future. Under the Consolidated Annual Contributions Contract, these activities may be considered events of substantial default.

BACKGROUND

The Petersburg Redevelopment and Housing Authority was established in 1968 to provide safe and sanitary housing for the low-income citizens of the city of Petersburg, Virginia. The Authority's mission is to serve its citizens by providing affordable housing opportunities in a safe environment, revitalizing and maintaining neighborhoods, providing opportunities for low and moderate-income homeownership, and continuing an active partnership with the city of Petersburg. The City Council appoints a seven-member Board of Commissioners to govern the Authority. The present Board Chairman is Robert Jones. The current Executive Director is Julian Marsh. The Authority is located at 128 South Sycamore Street in Petersburg, Virginia.

The Petersburg Redevelopment and Housing Authority owns and manages 479 public housing units under its Consolidated Annual Contributions Contract with HUD. The Consolidated Annual Contributions Contract defines the terms and conditions under which the Authority agrees to develop and operate all projects under the agreement. HUD provided the Authority the following financial assistance from Fiscal Years 1999 to 2002:

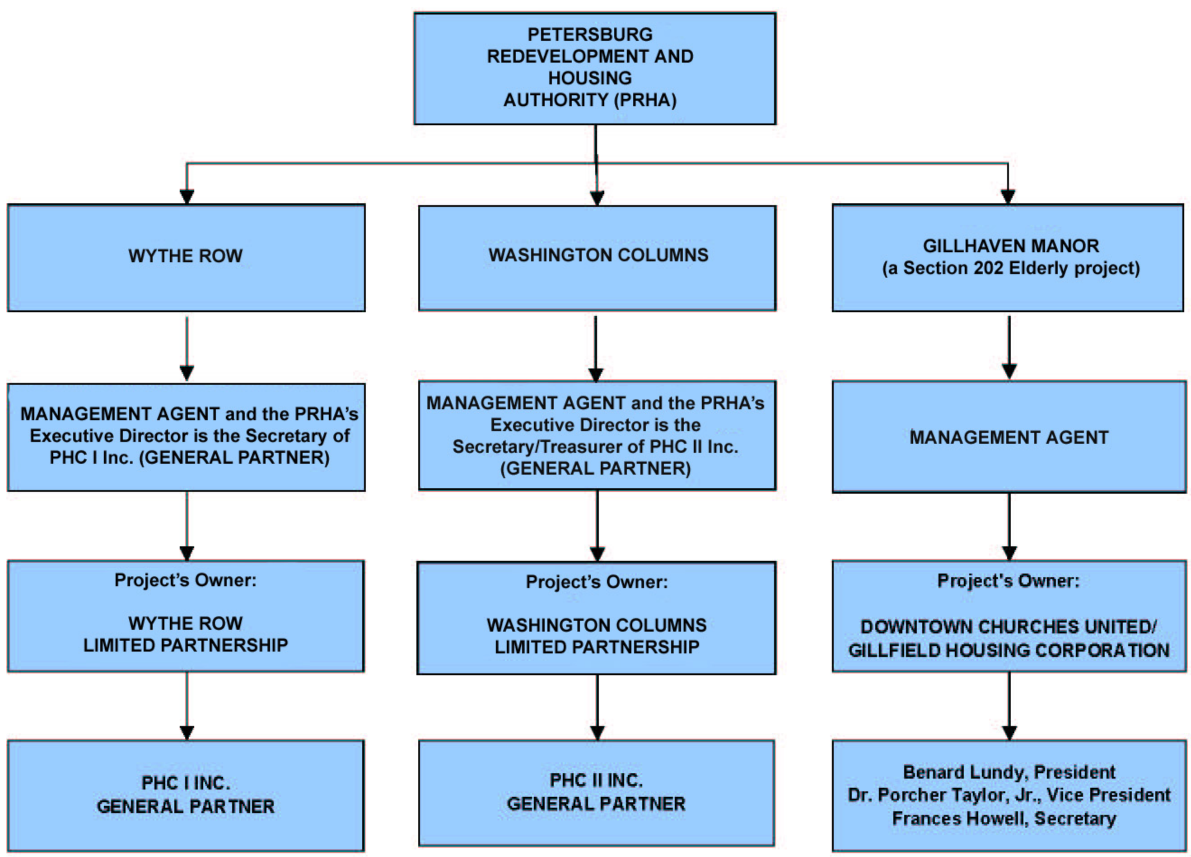
- $4.3 million Operating Subsidy to operate and maintain its housing developments.

- $3.4 million Capital Fund Program and Comprehensive Grant Program funding to modernize public housing units.

- $10.6 million to provide housing assistance through tenant-based Section 8 certificates and vouchers.

- $323,430 Public Housing Drug Elimination Program funds to eliminate or reduce drug related crime and other major crime and disorder problems.

Virginia state law also allows housing authorities to form non-stock and nonprofit entities for the purpose of developing low-income housing outside of HUD. In addition to the projects under its Consolidated Annual Contributions Contract with HUD, the Authority established the Petersburg Housing Corporation in April 1992 to develop nonfederal low-income housing projects. Two non-stock corporations known as Petersburg Housing Corporation I and II later replaced the Petersburg Housing Corporation as the general partners for the Authority's nonfederal housing projects. The Authority also currently acts as the management agent for a third nonfederal project. In total, the Authority manages an additional 138 units outside of HUD at the three projects. The current relationship between the Authority and its affiliated nonfederal entities is shown below:



Authority officials created the Wythe Row Limited Partnership to acquire, finance, rehabilitate, construct, own, operate and lease 12 units of low- and moderate-income housing. The Authority formed the Washington Columns Limited Partnership to develop, construct, own, maintain and operate a 26-unit project for rental to elderly persons of low-income. This Limited Partnership also rehabilitated the Robert E. Lee School building and "Blue House" on West Washington Street. Officials also created separate Petersburg Housing Corporations (PHC) to act as general partners for Wythe Row and Washington Columns. Additionally, the Authority is the management agent for Gillhaven Manor, a Section 202 Project[1] containing one hundred housing units. Downtown Churches United and the Gillfield Housing Corporation own Gillhaven Manor.

FINDING

THE AUTHORITY IMPROPERLY USED FEDERAL FUNDS TO SUPPORT ITS AFFILIATED NONFEDERAL ENTITIES

The Authority used federal funds improperly on a regular basis to support its affiliated nonfederal entities and also improperly pledged assets to guarantee the debt of two of its three affiliated nonfederal housing projects. This occurred because it did not properly account for work its employees performed and did not take measures to ensure Authority assets were not encumbered or pledged without HUD approval. Specifically, officials did not prepare personnel activity reports or time sheets for services performed by the Executive Director, management staff, all accounting personnel, the Human Resources Specialist, and some maintenance personnel. The Authority's management turnover, inadequate financial system, and potential conflicts of interest contributed to these problems.

The Authority's encumbering of assets without HUD approval may constitute grounds for a declaration of substantial default of its Consolidated Annual Contributions Contract with HUD. Further, the Authority violated the conflict of interest provisions of its Contributions Contract. As a result, the Authority improperly guaranteed debt incurred by its nonfederal entities estimated at $950,318. Additionally, it improperly paid salaries estimated at $620,236 from federal funds for work its employees performed in support of its affiliated nonfederal housing projects on a part-time basis from January 2001 until December 2003. Further, we estimated the Authority could more effectively utilize another $370,415 annually by ensuring it was properly accounting for and receiving reimbursement for work its employees performed for its affiliated nonfederal housing projects, and by preventing apparent conflict of interest situations in the future. Under the Consolidated Annual Contributions Contract, these activities may be considered events of substantial default.

The Authority Improperly Pledged Annual Contributions Contract Assets

The Authority violated its Annual Contributions Contract by guaranteeing debt, estimated at $950,318, of its affiliated nonfederal housing projects. In so doing, the Authority placed federal funds at risk by improperly pledging assets covered by the contributions contract without prior approval from HUD. Encumbering assets, or pledging Annual Contributions Contract assets as collateral for a loan, constitutes grounds for a declaration of substantial default of the contributions contract[1]. To illustrate:

- The Chairman of the Board of the Authority signed an agreement in May 1999, which obligated the Authority to absolutely and unconditionally guarantee all of the debt of the Wythe Row Limited Partnership. According to a document attached to the Wythe Row Limited Partnership Agreement entitled "Affiliate Guaranty", the Petersburg Redevelopment and Housing Authority is responsible for all the "indebtedness" of the Wythe Row Limited Partnership. The document did not identify what assets the Authority would use in the event it was required to pay off the Partnership's current or future debts. By signing this absolute and unconditional guarantee of all of the debt of the Wythe Row Limited Partnership however, the Chairman of the Board created an unknown and potentially large contingent liability, and placed the Authority's assets at substantial risk. While the future indebtedness of Wythe Row Limited Partnership is unknown at this time, our review of financial records showed that as of November 2003, the Partnership owed $550,318 to its creditors.

- The Chairman of the Board of the Authority signed a Promissory Note while also serving as the President of the Petersburg Housing Corporation in February 2002. The note required the Authority to pay $400,000 of the Washington Columns Limited Partnership debt should it go into default. The document did not identify which assets the Authority would use to pay the debt. As a result, the Authority placed federal funds at substantial risk, in non-compliance with the Annual Contributions Contract.

The Authority's Executive Director could not tell us or provide documentation identifying what Authority assets would be used to cover these contingent liabilities. In the absence of documents identifying the funds that would be used to pay these contingent liabilities, there is substantial risk to the Authority's Annual Contributions Contract assets if the entities go into default.

The Authority Did Not Properly Account for All Personnel Services It Provided to Its Nonfederal Entities

According to the Authority's financial records as of August 2003, its nonfederal entities owed the Authority $102,570 for work Authority employees performed on a full-time basis to support the nonfederal entities. These expenses consisted primarily of salaries and fringe benefits for two Authority employees who worked full-time at Washington Columns and five Authority employees who worked full-time at Gillhaven Manor. However, during our review we found the Authority used a number of other employees, on a part-time basis, to provide significant support to its nonfederal projects that it did not properly account for in its books. Specifically, the Authority failed to prepare personnel

[1] Section 17 – Notices, Defaults, Remedies

activity reports or time sheets to support services performed by the Executive Director, management staff, accounting personnel, human resources specialist, and several maintenance personnel. In total we estimate the Authority paid $620,236 from its Annual Contributions Contract funds from January 2001 until December 2003 for salary and benefits for Authority employees who worked to support the nonfederal housing developments. As such, in the future we estimate the Authority will be able to use $206,745[2] more effectively on an annual basis by properly accounting for the work of its employees.

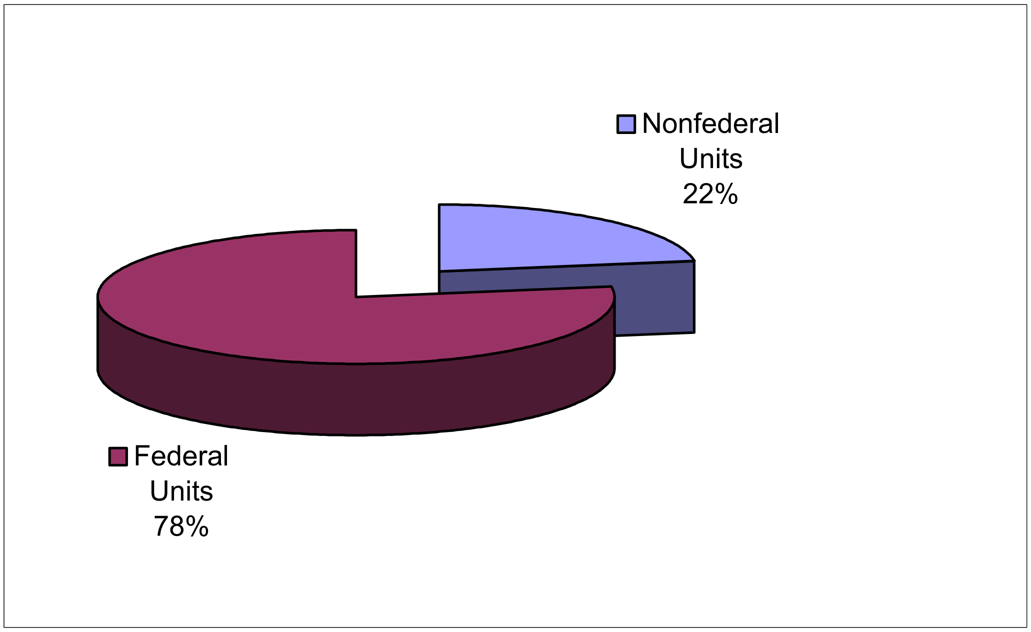
The Authority's Consolidated Annual Contributions Contract with HUD requires it to maintain records that identify the source and allocation of its funds. This key management control is critical in order to ensure the Authority spends federal funds, provided through its Annual Contributions Contract, only in accordance with the regulatory requirements of each specific federal program. Further, the contract specifies that the Authority can only withdraw federal funds for the payment of costs associated with the development and operation of projects under its Annual Contributions Contract or other projects specifically approved by HUD. Thus, when employees work on multiple programs, a distribution of their salaries should be supported by personnel reports or equivalent documentation.

Further, the Office of Management and Budget Circular A-87 requires the Authority to assign costs to benefited activities on a reasonable and consistent basis. Formal accounting and other records should support all costs and other data used to distribute the costs included in its cost allocation plan, including the support needed to establish the propriety of the costs assigned to the federal awards.

Authority officials told us that since their affiliated nonfederal entities did not have their own employees, these entities relied on the Authority's employees to provide much of the needed support. However, in doing so without properly reimbursing the Authority, officials improperly used federal funds to sustain their affiliated nonfederal entities and violated the terms of their Annual Contributions Contract with HUD.

Since the Authority did not have an allocation plan or maintain time sheets to properly account for work its employees performed at both its federal and nonfederal properties, we estimated the total salary and fringe benefits that the low-income housing fund paid to support the nonfederal entities. Our estimate was calculated by multiplying the total salary and benefits costs, that were paid to the individuals we identified as having worked on both the federal and nonfederal, by the percentage the nonfederal units comprised of the total units under the Authority's management. We found the Authority managed a total of 617 low-income housing units and that 138 of these units were not covered by its Annual Contributions Contract. As illustrated below, the percentage of employee salaries that should have been fairly allocated to the nonfederal entities was 22-percent (138 nonfederal units divided by 617 total units).

[2] $620,236 divided by 3 years equals $206,745 per year.



Based on the accounting records of the Authority, total salaries and benefits paid to these individuals from January 2001 through December 2003 totaled $2,819,255. Since the nonfederal units under management accounted for 22-percent of the Authority's total units, we calculated the ineligible payments to be $620,236.

Nonfederal Entities Owed the Authority Over $100,000 for Full-time Support

As previously discussed, the Authority's nonfederal entities owed the Authority $102,570 for work Authority employees performed on a full-time or dedicated basis. These expenses consisted primarily of salaries and fringe benefits of two Authority employees dedicated to Washington Columns and five Authority employees working full-time at Gillhaven Manor. As of August 2003, the three nonfederal entities owed the following:

Nonfederal Project	Amount
Washington Columns	$ 69,214
Gillhaven Manor	$ 29,103
Wythe Row	$ 4,253
Total	$102,570

The Authority used a due from/due to accounting system to account for expenses of its nonfederal entities, including salaries and benefits of its employees working for the nonfederal entities full-time. Housing authorities typically use this system when they pay obligations for more than one program or entity from a general fund/revolving fund. They may also use such accounting for transactions directly between other funds and/or other entities included within the general ledger. A program or entity's due-to balance represents amounts it owes (payable) another fund or entity for disbursements and/or advances made in its behalf. Conversely, a due-from balance (receivable) represents an amount owed the entity. The Authority should ensure that its balances due from its nonfederal entities are settled on a monthly basis and not carried forward.

The Authority should take immediate action to recover the $102,570 it is owed from its nonfederal entities. Our review showed the Authority was regularly owed similar large balances from its affiliated nonfederal entities since at least January 2001. Thus, we estimated that in the future, the Authority will be able to use an estimated $102,570 more effectively on an annual basis by ensuring that balances due from its nonfederal entities are settled on a monthly basis and not carried forward for its employees working full-time in support of its nonfederal housing projects.

Management Turnover Exacerbated Accounting Problems

The Authority had major turnover in key management positions that contributed significantly to its accounting problems. For example, the Authority has been without a Finance Director for over seven months (since June 2003). During 2002 and 2003, three different individuals held the position of Finance Director. The Authority removed one of those individuals from the position because of problems associated with its Fiscal Year 2000 financial audit. The next Finance Director served only six months. She was replaced by an individual who was also serving as Vice Mayor of Petersburg. This individual resigned in June 2003 because of apparent conflicts of interest identified by our audit (discussed below).

Our review also showed the Authority's accounting system did not always produce reliable data. Specifically, the interfund due to the low-income housing fund in the Fiscal Year 2001 audit of the Authority's financial statements did not agree with either the electronic or hard copy data. Additionally, we could not adequately track funds owed to the Authority by the nonfederal entities. We believe the turnover of key financial management personnel and the failure of the Authority to fill the position timely contributed to a great extent to the Authority's inability to produce reliable historical financial data. We will address problems associated with the Authority's inadequate financial system and other related audit issues in greater detail in a subsequent audit report.

Apparent Conflicts of Interest Existed

Our audit also identified apparent conflicts of interest at the Authority. The Consolidated Annual Contributions Contract prohibits the Authority from entering into any contract or arrangement in connection with any project under the contract in which several classes of people have an interest, direct and indirect, during his or her tenure or for one year thereafter. These classes include any present or former member or officer of the governing body of the Authority, any Authority employee who formulates policy or who influences decisions with respect to the project(s), and any public official who exercises functions or responsibilities with respect to the project(s) or the Authority.

During the audit we found that the Authority's Finance Director was also serving as the Vice Mayor of the City of Petersburg. In addition to the apparent conflicting priorities of the positions, the individual was earning compensation and had a financial interest in both positions. Therefore, in our opinion, an apparent conflict of interest situation existed. After we raised concerns about potential conflicts of interest with this arrangement, he attempted to obtain a waiver of this requirement from HUD. HUD declined the waiver request however, and the individual was required to resign as Finance Director. Since the individual's salary and benefits as Finance Director were valued at about $61,100 annually, we believe these are funds that the Authority can put to better use in the future by preventing apparent conflict of interest situations.

We further found that another apparent conflict of interest situation may have occurred because the Chairman of the Board of the Authority signed a Guaranty Agreement and a Promissory Note while also serving as the President of its affiliated nonstock corporations. As stated previously, the Consolidated Annual Contributions Contract prohibits the Authority from entering into any contract or arrangement in connection with any project under the contract in which an officer of the governing body of the Authority has an interest, direct and indirect. While HUD is permitted to waive this requirement for good cause, the Authority did not obtain the needed waiver.

In our opinion, the Authority's practice of allowing key Authority personnel to serve in similar roles for its nonfederal entities contributed to its problems. By allowing this practice, and not implementing effective controls to compensate for it, the Authority accepted substantial and unacceptable risk to its assets. The Authority could have mitigated much of this risk however, by obtaining a formal resolution from its Board of Commissioners and requesting HUD approval authorizing these agreements guaranteeing the debt of its affiliated nonfederal entities. It did not do so. Regrettably, in addition to the apparent conflict of interest, these agreements improperly encumbered Consolidated Annual Contributions Contract assets estimated at $950,318 without HUD or Board approval.

New Executive Director Appointed in April 2003

In April 2003, the Board of Commissioners appointed a new Executive Director who inherited major challenges. While the current accounting staff and the newly appointed Executive Director expressed a desire to correct the Authority's deficiencies, they could not adequately explain why the Authority does not adequately or accurately account for and allocate costs. They also could not tell us what assets the Authority would use to cover its contingent liabilities. In summary, we believe the Authority's failure to properly allocate and account for significant costs related to accounting, maintenance and other services it provided to its nonfederal entities, and its pledging of future Consolidated Annual Contributions Contract assets, may be grounds for a declaration of substantial default of its contract with HUD.

AUDITEE COMMENTS

We discussed the draft findings with Authority personnel during the audit, and at an exit conference with the Executive Director on February 23, 2004. The Authority provided written comments to our draft findings on March 12, 2004. In its response, the Authority acknowledged it needed to take action to ensure it did not improperly pledge Consolidated Annual Contributions Contract assets, and to ensure it properly accounted for all personnel services it provided to its nonfederal entities. The Authority also agreed its management turnover exacerbated its accounting problems, and it did not properly bill or collect funds owed by its nonfederal entities. The Authority further acknowledged it needed to take action to ensure apparent conflicts of interest did not exist.

The Authority stated it recently hired a consultant to prepare a cost allocation plan. Based on this newly created allocation plan, and its belief it received management fees from the entities, the Authority stated it earned a profit for providing services through its nonfederal entities. The Authority also stated that going forward, it would ensure it used only nonfederal assets to guarantee debt incurred by its nonfederal entities, and it would consult with HUD whenever it perceives an apparent conflict of interest. Lastly, the Authority stated it would begin billing and collecting funds owed by its nonfederal entities on monthly basis.

OIG EVALUATION OF AUDITEE COMMENTS

We considered the Authority's comments in preparing the final report and included the full narrative portion of its response, without attachments, as Appendix B. The Authority's complete response, including attachments, is available upon request.

We are encouraged that the Authority acknowledged the management control weaknesses our audit identified, and has begun taking actions to strengthen its management controls. However, we question the Authority's assertion that it made a profit for providing services through its nonfederal entities. In this regard, we reviewed the cost allocation plan the Authority's consultant provided us at our exit conference.

During our audit we found the Authority used a number of employees, on a part-time basis, to provide significant support to its nonfederal projects that it did not properly account for in its books. However, the plan submitted by the Authority did not account for these employees. Further, in its written response, the Authority acknowledged that its financial records have been in disarray. In this regard, the Authority could not support its claim that it received management fees from its nonfederal entities. The Authority's inability to support that it received management fees, coupled with its failure to allocate all relevant costs, cast significant doubt on its contention that it realized a profit from its nonfederal entities. On the contrary, our audit showed the Authority provided significant assistance to these entities using federal assets.

RECOMMENDATIONS

We recommend that HUD:

1A. Require the Authority to take immediate action to withdraw its pledge of Consolidated Annual Contributions Contract assets.

1B. Take appropriate administrative action against the Chairmen of the Authority's Board of Commissioners responsible for pledging assets covered by the Consolidated Annual Contributions Contract without prior approval from HUD.

1C. Require the Authority to submit all agreements in which it is guaranteeing debt to HUD for approval and ensure that its assets are not encumbered or pledged without HUD approval in the future.

1D. Review issues contained in this audit report, and if appropriate, initiate action to declare the Authority in substantial default of its Consolidated Annual Contributions Contract, and take appropriate administrative action as detailed in Section 17 (Notices, Defaults and Remedies) of the Contract.

1E. Require the Authority to recover $620,236 from its nonfederal entities for employee expenses not properly allocated to the nonfederal entities or repay it from nonfederal funds.

1F. Require the Authority to develop a reasonable method for allocating its future costs to include preparing personnel activity reports or time sheets for services performed by its employees.

1G. Require the Authority to recover $102,570 from its nonfederal entities for work performed by its employees on a full-time basis in support of the entities or repay it from nonfederal funds.

1H. Require the Authority to ensure that its due-from balances are settled on a monthly basis and not carried forward.

1I. Require the Authority's Board of Commissioners to implement appropriate measures to prevent and resolve apparent conflict of interest situations.

1J. Require the Authority's Board of Commissioners to establish controls to monitor Authority interactions with its affiliated nonfederal entities and ensure transactions comply with its Consolidated Annual Contributions Contract and other HUD requirements.

MANAGEMENT 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 policies, procedures, control systems, and other management tools implemented to ensure that the nonfederal entities pay for all the services provided by the Authority were relevant to our audit objective. 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:

The Authority did not:

- Properly account for services performed by its management and staff personnel for its nonfederal entities.

- Ensure that its nonfederal entities pay for all services provided by the Authority.

- Ensure that its Annual Contributions Contract assets are not encumbered or pledged without HUD approval.

- Ensure that its due-from balances are settled on a monthly basis and not carried forward.

- Ensure it took appropriate measures to prevent and resolve apparent conflict of interest situations.

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation Number	Ineligible Costs 1/	Funds Put to Better Use 2/
1A		$ 950,318
1E	$620,236	
1F		$ 206,745
1G		$ 102,570
1I		$ 61,100
Total	$620,236	$1,320,733

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that are not allowed by law, contract, or federal, state or local policies or regulations.

2/ Funds put to better use quantify monetary savings from management actions that prevent improper obligations or expenditures of agency funds or avoid unnecessary expenditures.

AUDITEE COMMENTS

REDEVELOPMENT AND HOUSING AUTHORITY
PETERSBURG
EST. 1968

Petersburg Redevelopment & Housing Authority

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Petersburg, Virginia 23803

Phone 804.733.2200 Fax 804.733.2229

March 12, 2004

Mr. Daniel G. Temme
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Wanamaker Building, suite 1005
100 Pen Square East
Philadelphia, PA 19107-3380

Re: Draft Audit Memorandum Report dated February 26, 2004

Dear Mr. Temme:

The above-referenced report has been reviewed by the management of the Petersburg Redevelopment and Housing Authority ("PRHA"). In response to each proposed finding in the Report, we ask that you consider the following:

The Authority Improperly Pledged Annual Contributions Contract Assets.

PRHA guaranteed the debt of the Wythe Row Limited Partnership ("WRLP") which guaranty declines over time and, as to the Washington Columns Limited Partnership ("WCLP"), PRHA agreed to loan up to $400,000 from nonfederal Homes Sales monies, for a period of 10 years to Petersburg Housing Corporation to support the guaranty of Petersburg Housing Corporation ("PHC") of the financial obligations of the general partner (PHC-II, Inc.) of WCLP. The PRHA Board of Commissioners never approved the guaranty for WRLP. Both PHC and PHC-II, Inc. are affiliates of PRHA.

In November, 2003, WRLP owed $550,318 to its creditors, all of which debt was current. In the case of WRLP, there was no indication of which PRHA funds would be used to collateralize the guaranty. PRHA did, however, have $1,255,446 in its "Home Sales" accounts at that time. Therefore, these nonfederal funds were available to collateralize both guaranties. There has been no financial default involving either WRLP or WCLP and, accordingly, no call upon the guaranties.

2.

PRHA has now negotiated with the Virginia Community Development Corporation, the purchaser of the tax credits for these two developments, a substantial reduction in the amount of the guarantees. The changes that have been agreed to would limit the operating loan deficit guaranty to $50,000 on WRLP and to $200,000 on WCLP, unless the entities must retain a third party management company other than PRHA to manage these developments. The tax credit guaranty on WRLP has been reduced from $860,000 to $250,000. Only the $50,000 for WRLP would be required to be collaterized with cash, specifically earmarked to come from the Home Sales accounts. The $200,000 guaranteed to WCLP is not a cash guaranty, but rather a pledge of future development fees not yet paid to PRHA. No other guaranties on these two developments are required by Virginia Community Development Corporation to be collateralized. Copies of correspondence from our legal counsel and Virginia Community Development Corporation are enclosed as "Attachment A" and "Attachment B" for your review.

The Authority Did Not Properly Account For All Personnel Services it Provided To Its Nonfederal Entities.

PRHA did not account for personnel services provided to its nonfederal entities during 2001 and 2002. For 2003, however, PRHA put in place a proper allocation system and expenses have been allocated, and PRHA will bill and seek reimbursement for all such expenses. Rather than use a straight 22% percent (the percentage of non-affiliated entity units managed compared to the total number of PRHA units managed) as proposed in the Report, for 2001 and 2002 an analysis of the actual time spent by PRHA employees has been prepared. A memorandum from Alan G. Reese of A. G. Reese & Associates, P.C., enclosed as "Attachment C", outlines the results of the analysis. Based on this analysis, the payroll allocation for work performed for nonfederal affiliates of PRHA is $38,180 for 2001 and $51,551 for 2002.

During 2001 and 2002, PRHA received Management Fees totaling $50,771 and $54,792. Additionally, a development fee of $421,286 was earned from WCLP in 2002. Based on these figures, PRHA has earned a profit for providing services through its personnel to these nonfederal entities.

Nonfederal Entities Owed the Authority Over $100,000 for Full-Time Support.

Salaries and expenses of the PRHA employees working at Washington Columns and Gillhaven are required to be reimbursed to PRHA. Funds owed by those entities have now been paid to PRHA, and will be billed and collected on a monthly basis going forward.

Management Turnover Exacerbated Accounting Problems

There has been a significant turnover of Finance Directors over the past three years. Because of that turnover, the financial records have been in disarray. The new Executive

Director did not want to bring a new Finance Director into an organization with severe record keeping problems. With the help of consultants (Casterline Associates, P.C. and A.G. Reese & Associates, P.C.), the records are now in much better shape. The search for a new Finance Director has begun and it is hoped the position will be filled soon.

Apparent Conflicts of Interest Existed

Conflicts of interest have existed in the past. The current management of PRHA will assure that those conflicts do not continue in the future. The local HUD office will be consulted whenever an apparent or potential conflict is perceived.

New Executive Director Appointed in April 2003

The new Executive Director has had the above mentioned consultants prepare a proper cost allocation plan. Also, by negotiating with Virginia Community Development Corporation, the amount of the guarantees has been reduced significantly, and non federal assets are used to collateralize the guarantees.

In addition to the above mentioned items PRHA has implemented, or is implementing, policies to assure that errors of the past are not continued into the future.Before any final recommendations are made by your office to HUD, PRHA would like to have the opportunity to review these recommendations to ensure that all of the facts underlying the recommendations are accurate.

We look forward to hearing from you at your earliest convenience.

Sincerely,

Julian Marsh/[illegible]

Julian Marsh
Executive Director