
AUDIT REPORT



NORTHSTAR COMMUNITY DEVELOPMENT
CORPORATION
ECONOMIC DEVELOPMENT INITIATIVE – SPECIAL
PURPOSE GRANT (B-02-SP-MI-0310)

DETROIT, MICHIGAN

NorthStar Inappropriately Used More Than \$120,000 in Grant
Funds and HUD's Interest in More Than \$180,000 in Grant
Funds Was Not Secured

2006-CH-1006

DECEMBER 30, 2005

OFFICE OF AUDIT, REGION V
CHICAGO, ILLINOIS



Issue Date	December 30, 2005
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Audit Report Number	2006-CH-1006
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TO: Francis P. McNally, Director of Congressional Grants, DECC
Jeanette Harris, Director of Community Planning and Development, 5FD

FROM: 
Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: NorthStar Community Development Corporation Inappropriately Used More Than \$120,000 in Economic Development Initiative - Special Purpose Grant Funds and HUD's Interest in More Than \$180,000 in Grant Funds Was Not Secured; Detroit, Michigan

HIGHLIGHTS

What We Audited and Why

We audited NorthStar Community Development Corporation's (NorthStar) Economic Development Initiative - Special Purpose Grant (Grant). We initiated the audit in conjunction with our internal review of the U.S. Department of Housing and Urban Development's (HUD) oversight of Economic Development Initiative - Special Purpose Grants. The review is part of our fiscal year 2005 annual audit plan. We chose NorthStar's Grant based upon a statistical sample of fiscal years 2002 and 2003 Economic Development Initiative - Special Purpose Grants, in which 90 percent or more in funds were disbursed. Our objectives were to determine whether NorthStar used its Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted properties.

What We Found

NorthStar improperly used \$123,372 in Grant funds from March 2002 through July 2005. The inappropriate expenses included \$49,200 to purchase 39 properties for Harmony Park; \$46,700 to pay engineering, environmental

assessment, and closing cost expenses for properties within Pilgrim Park Homes; \$13,106 in property taxes, including fines and penalties, for Community House; \$8,399 to pay for deeds and title work for properties of Revitalife; \$4,098 in rehabilitation for NorthStar's Center; and \$1,869 in property taxes for the property located at 15411 Rosa Parks Boulevard.

NorthStar lacked documentation to support that an additional \$1,970 in Grant funds was used according to NorthStar's amended budget approved by HUD. In addition, NorthStar used \$184,871 in Grant funds to acquire, or aid in the acquisition of, and/or rehabilitate real property; however, NorthStar did not place covenants on the properties' titles assuring nondiscrimination based on race, color, national origin, or handicap. Further, HUD did not request that NorthStar record HUD's interest on the properties' titles.

What We Recommend

We recommend that HUD's director of congressional grants require NorthStar to (1) reimburse HUD from nonfederal funds for the inappropriate expenses; (2) provide documentation to support the unsupported expenses or reimburse HUD from nonfederal funds for the applicable portion; (3) implement procedures and controls to address the deficiencies cited in this report; and (4) record covenants on the titles assuring nondiscrimination based on race, color, national origin, or handicap and record liens on the titles for the University Grove properties, NorthStar's Center, the Pilgrim Park properties, the Harmony Park properties, and the Revitalife properties showing HUD's interest in the assisted properties. If the covenants and liens are not recorded, NorthStar should reimburse HUD \$184,871 from nonfederal funds for the Grant funds used on these properties.

We also recommend that HUD's director of congressional grants, in conjunction with the director of HUD's Detroit Office of Community Planning and Development, determine whether NorthStar's expense documentation for other HUD-funded grants was used to support expenses of the Grant since they were awarded for some of the same activities.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided our discussion draft audit report to NorthStar's vice president and chief financial officer and HUD's staff during the audit. We held an exit conference with NorthStar's vice president and chief financial officer on December 19, 2005.

We asked NorthStar's vice president and chief financial officer to provide comments on our discussion draft audit report by December 24, 2005. NorthStar's vice president and chief financial officer provided written comments dated December 26, 2005. NorthStar's vice president and chief financial officer agreed to implement corrective actions to address our findings and provided documentation for unsupported disbursements relating to University Grove. The complete text of the written response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Economic Development Initiative program. The U.S. Department of Housing and Urban Development's (HUD) Economic Development Initiative program includes noncompetitive Economic Development Initiative – Special Purpose Grants. HUD awards Economic Development Initiative – Special Purpose Grants to entities included in the U.S. House of Representatives' conference reports.

NorthStar Community Development Corporation. Incorporated in 1986 as a nonprofit corporation under the laws of the State of Michigan, NorthStar Community Development Corporation (NorthStar) is governed by a nine-member board of directors. The U.S. House of Representatives' Conference Report 107-272 set aside \$350,000 in Economic Development Initiative – Special Purpose Grant (Grant) funds to NorthStar for a targeted housing production program. In August 2002, HUD awarded NorthStar the \$350,000 Grant for its Varsity Park Development Plan, consisting of two housing developments called University Grove and Pilgrim Village Homes; Community House, a mini substation for the Detroit Police Department; Titan Pointe, a housing development; Revitalife, a scattered-site housing program; and administrative expenses. HUD approved an amended budget for the \$350,000 Grant in October 2003. The table below contains the amended budget's expense items.

<i>Expense item</i>	<i>Budget amount</i>
Administrative	\$150,000
Community House rehabilitation	95,000
NorthStar's Center rehabilitation	60,000
University Grove predevelopment	<u>45,000</u>
<i>Total</i>	<u>\$350,000</u>

NorthStar increased its administrative expenses due to a reduction in Community Development Block Grant and HOME funds from the City of Detroit that funded the expenses; increased the rehabilitation costs for Community House due to continuing vandalism of the building; included NorthStar's Center rehabilitation costs to create a community development center; increased University Grove's predevelopment expenses because the actual costs were greater than the estimated costs; eliminated Pilgrim Village Homes due to finding an alternative funding source; eliminated Titan Pointe as a result of a delay in the project's start; and eliminated Revitalife because matching funds were unavailable. NorthStar's records for the Grant are located at 3800 Puritan Street, Detroit, Michigan.

We initiated this audit in conjunction with our internal review of HUD's oversight of Economic Development Initiative – Special Purpose Grants. The review is part of our fiscal year 2005 annual audit plan. We chose NorthStar's Grant based upon a statistical sample of fiscal years 2002 and 2003 Economic Development Initiative – Special Purpose Grants, in which 90 percent or more in funds were disbursed.

Our objectives were to determine whether the NorthStar used its Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted properties.

RESULTS OF AUDIT

Finding 1: NorthStar Inappropriately Used More Than \$120,000 in Grant Funds

NorthStar improperly used \$123,372 in Grant funds from March 2002 through July 2005. The inappropriate expenses included \$49,200 to purchase 39 properties for Harmony Park; \$46,700 to pay engineering, environmental assessment, and closing cost expenses for properties within Pilgrim Park Homes; \$13,106 in property taxes, including fines and penalties, for Community House; \$8,399 to pay for deeds and title work for Revitalife's properties; \$4,098 in rehabilitation for NorthStar's Center; and \$1,869 in property taxes for the property located at 15411 Rosa Parks Boulevard. NorthStar lacked documentation to support that an additional \$1,970 in Grant funds was used according to NorthStar's amended budget. We provided NorthStar schedules of the inappropriate and unsupported payments. The problems occurred because NorthStar lacked effective procedures and controls over the use of Grant funds. As a result, Grant funds were not used efficiently and effectively.

NorthStar Inappropriately Used More Than \$120,000 in Grant Funds

Contrary to article I, section A, of its grant agreement, NorthStar used \$123,372 in Grant funds for expenses not included in its amended budget approved by HUD. The disbursements occurred from March 2002 through July 2005. NorthStar's amended budget included the following expenses: \$150,000 for administration; \$95,000 for Community House rehabilitation; \$60,000 for NorthStar's Center rehabilitation; and \$45,000 for University Grove predevelopment. However, NorthStar improperly: used \$49,200 to purchase 39 properties for Harmony Park; paid engineering, environmental assessment, and closing cost expenses totaling \$46,700 for properties within Pilgrim Park Homes; paid property taxes, including fines and penalties, totaling \$13,106 for Community House; used \$8,399 to pay for deeds and title work for properties of Revitalife; paid \$4,098 in rehabilitation for NorthStar's Center; and used \$1,869 to pay property taxes for the property located at 15411 Rosa Parks Boulevard.

Further, NorthStar lacked documentation to support that an additional \$1,970 in Grant funds was used according to NorthStar's amended budget. The unsupported disbursements, which related to University Grove, included \$470 in acquisition costs for the property located at 15710 Dexter Avenue, and \$1,500 for a tax credit application to the Michigan State Housing Development Authority.

NorthStar used \$148,184 in Grant funds to pay administrative expenses, had not started the rehabilitation of Community House, and exceeded its amended budget amount for NorthStar's Center by \$4,098. We were unable to determine whether NorthStar completed the \$45,000 in predevelopment for University Grove using both Grant and other funds since NorthStar lacked supporting documentation and University Grove was a scattered-site housing development.

NorthStar Lacked Effective Controls Over the Grant Funds

NorthStar's vice president and chief financial officer said NorthStar's work revolves around its Varsity Park Development Plan. All of the funds were used for projects included in the Varsity Park Development Plan. Therefore, it does not matter for which project the funds were used. The misuse of Grant funds occurred because NorthStar lacked effective procedures and controls over the Grant. As a result, HUD's Grant funds were not used effectively and efficiently.

NorthStar submitted a revised budget for the Grant dated December 13, 2005, to HUD. The director of HUD's Office of Congressional Grants denied NorthStar's request since all Grant funds were disbursed prior to the submission of the revised budget.

NorthStar Also Received Block Grant and HOME Funds

NorthStar provided supporting documentation for the Grant funds totaling \$148,184 in administrative expenses, which included \$16,631 and \$131,553 for expenses incurred in 2002 and 2003, respectively. However, NorthStar's independent public accountant's workpapers showed Grant funds were used to pay for NorthStar's administrative expenses totaling \$50,000 and \$100,000 for 2002 and 2003, respectively. NorthStar received an additional \$1,035,640 in Community Development Block Grant (Block Grant) and HOME Investment Partnerships Program (HOME) funds to pay for salaries from July 1, 2002, through September 30, 2005. The following table details the grant type, number, period, and amount for salaries.

<i>Type</i>	<i>Number</i>	<i>Period</i>	<i>Amount</i>
Block Grant	2606578	7/1/02 – 6/30/03	\$492,265
Block Grant	2638883	7/1/03 – 6/30/04	263,700
HOME	2640145	10/1/02 – 9/30/05	225,000
Block Grant	2651997	7/1/03 – 6/30/04	<u>54,675</u>
Totals			<u>\$1,035,640</u>

Further, NorthStar was awarded \$85,000 in Block Grant (number 2620880) funds for the period January 28, 2004, through January 27, 2006, for Media Center's rehabilitation. Since NorthStar received multiple HUD funds to pay similar expenses during the same periods, HUD lacks assurance that its funds were not inappropriately used to pay the similar expenses for another grant.

Recommendations

We recommend that HUD's director of congressional grants require NorthStar to

- 1A. Reimburse HUD from nonfederal funds for the \$123,372 in Grant funds cited in this finding that were not used in accordance with its amended budget approved by HUD.
- 1B. Provide documentation to support \$1,970 in unsupported expenses cited in this finding. If the necessary documentation cannot be provided, NorthStar should reimburse HUD from nonfederal funds for the applicable portion.
- 1C. Implement procedures and controls to ensure Grant funds are used according to its amended budget approved by HUD.

We recommend that HUD's director of congressional grants, in conjunction with the director of HUD's Detroit Office of Community Planning and Development

- 1D. Determine whether NorthStar's expense documentation for other HUD-funded grants was used to support expenses of the Grant since they were awarded for some of the same activities. If NorthStar used multiple grants to pay the same expenses, HUD should take appropriate action, including but not limited to reimbursement by NorthStar for the applicable amount and/or administrative action.

Finding 2: HUD's Interest in More Than \$180,000 in Grant Funds Awarded to NorthStar Was Not Secured

NorthStar used \$184,871 in Grant funds to acquire, or aid in the acquisition of, and/or rehabilitate real property; however, NorthStar did not place covenants on the properties' titles assuring nondiscrimination based on race, color, national origin, or handicap. NorthStar used: \$64,098 for rehabilitation of NorthStar's Center; \$49,200 to purchase 39 properties for Harmony Park; \$46,700 for engineering, environmental assessment, and closing costs for properties within Pilgrim Park Homes; \$16,474 for title work, architectural fees, environmental assessment, market study, and closing costs for University Grove properties; and \$8,399 for deeds and title work for properties of Revitalife. Further, HUD did not request that NorthStar record HUD's interest on the properties' titles. NorthStar did not record the covenants on the titles because it lacked effective oversight of the Grant. As a result, HUD's interest in the properties is not protected.

NorthStar Used More Than \$180,000 in Grant Funds without Placing Covenants on the Properties' Titles to Ensure Nondiscrimination

Contary to federal requirements, NorthStar did not secure HUD's interest in \$184,871 in Grant funds used to acquire, or aid in the acquisition of, and/or rehabilitate real property. NorthStar paid \$64,098 for rehabilitation of NorthStar's Center; \$49,200 to purchase 39 properties for Harmony Park; \$46,700 for engineering, environmental assessment, and closing costs for properties within Pilgrim Park Homes; \$16,474 for title work, architectural fees, environmental assessment, market study, and closing costs for University Grove properties; and \$8,399 to pay for deeds and title work for properties of Revitalife. The Grant funds were disbursed from September 19, 2002, through June 15, 2005.

NorthStar failed to place covenants on the properties' titles to assure nondiscrimination based on race, color, national origin, or handicap. The purpose of the covenants is to ensure nondiscrimination for the period that the properties are used as outlined in NorthStar's application for the Grant or for another purpose involving similar services or benefits. The recording of the covenants will provide HUD recourse if discrimination based on race, color, national origin, or handicap occurs in relation to the properties.

HUD's Interest in the Properties Is at Risk

NorthStar's vice president and chief financial officer said HUD did not provide NorthStar any directives or guidance regarding the securing of HUD's interest in the properties. However, NorthStar assured HUD that it would place a covenant on the properties' titles to assure nondiscrimination during the useful life of the projects. The recording of the covenants will provide HUD recourse if discrimination based on race, color, national origin, or handicap occurs in relation to the properties.

HUD Did Not Request NorthStar to Record HUD's Interest on the Properties' Titles

HUD did not request NorthStar to record HUD's interest on the properties' titles. The recording of HUD's interest on the properties will help protect HUD in case the properties are sold or no longer used for their intended purpose. NorthStar's president certified in Standard Form 424D, Assurances – Construction Programs, section 3, that NorthStar would record the federal interest in the title of real property in accordance with awarding agency directives.

HUD's Office of Congressional Grants' position is that the standard form only requires NorthStar to record HUD's interest in the properties if HUD issued a directive that requires applicants to record HUD's interest in real property or HUD specifically directs NorthStar to record HUD's interest in the properties. HUD did not issue any directives requiring grant recipients to record HUD's interest in real property or specifically direct NorthStar to record HUD's interest. However, HUD clearly has the authority to require a grantee to record HUD's interest in an assisted property. Therefore, HUD's interest in the properties is not protected in case they are sold or are no longer used for their intended purpose.

Recommendations

We recommend that HUD's director of congressional grants require NorthStar to

- 2A. Record covenants on the properties' titles assuring nondiscrimination based on race, color, national origin, or handicap and record liens for NorthStar's Center, Harmony Park, Pilgrim Park Homes, Revitalife, and University Grove showing HUD's interest in the assisted properties. The covenants and liens should help ensure that NorthStar protects HUD's interest in the \$184,871 in Grant funds used for the properties.

- 2B. Reimburse HUD from nonfederal funds for the Grant funds used to pay for NorthStar's Center, Harmony Park, Pilgrim Park Homes, Revitalife, and University Grove properties if the covenants and liens are not recorded.

SCOPE AND METHODOLOGY

We performed the audit at the NorthStar's Center, Community House, and the University Grove properties during September and October 2005. To accomplish our objectives, we interviewed HUD's staff and NorthStar's employees.

To determine whether NorthStar used Grant funds in accordance with HUD's requirements and recorded HUD's interest on the assisted property, we reviewed:

- U.S. House of Representatives' Conference Report 107-272,
- HUD's file related to the Grant,
- NorthStar's financial records,
- Block Grants and HOME grants involving NorthStar,
- NorthStar's fiscal year 2003 audited financial statements, and
- The Michigan secretary of state's Website for organizational information on NorthStar.

We also reviewed 24 CFR [*Code of Federal Regulations*] Parts 1, 8, and 84; 56 *Federal Register* 16337; 70 *Federal Register* 35967; HUD Directives 1.5, 8.50, and 84.32; Office of Management and Budget Circulars A-21, A-87, A-110, and A-122; and HUD Handbook 2000.06, REV-3.

The audit covered the period from August 9, 2002, through August 31, 2005. This period was adjusted as necessary. We performed our audit in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

- Effectiveness and efficiency of operations,
- Reliability of financial reporting,
- Compliance with applicable laws and regulations, and
- Safeguarding resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed all of the relevant controls identified above.

A significant weakness exists if internal controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

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

- NorthStar inappropriately used Grant funds because it lacked effective procedures and controls over the Grant (see finding 1).
- NorthStar did not record the covenants on the titles because it lacked effective oversight of the Grant (see finding 2).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 2/
1A	<u>\$123,372</u>		
1B		<u>\$1,970</u>	
2A			<u>\$184,871</u>
Totals	<u>\$123,372</u>	<u>\$1,970</u>	<u>\$184,871</u>

- 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 those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of audit. 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 dDepartmental policies and procedures.
- 3/ “Funds to be put to better use” are quantifiable savings that are anticipated to occur if an Office of Inspector General (OIG) recommendation is implemented, resulting in reduced expenditures at a later time for the activities in question. This includes costs not incurred, deobligation of funds, withdrawal of interest, reductions in outlays, avoidance of unnecessary expenditures, loans and guarantees not made, and other savings.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



A Community Development Corporation

December 26, 2005

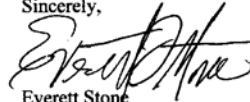
Brent G. Bowen
Assistant Regional Inspector General for Audit
U. S. Department of Housing and Urban Development
77 W. Jackson Blvd., Suite 2646
Metcalf Federal Building
Chicago, IL 60604

Dear Mr. Bowen:

Attached are NorthStar Community Development Corporation's comments to your audit findings on the review work of the Special Purpose Grant (B-02-SP-MI-0310). The fundamental purpose of these comments is to convey NorthStar's understanding of your findings and to express our perspective as it relates to these findings and the implementation of The University Commons Development Plan.

We are looking forward to the results of your evaluation of our comments. If you have any questions, please contact Lisa Tucker at (313) 341-9088.

Sincerely,



Everett Stone
Vice President and Chief Financial
Officer

Attachments

Comments on Review Work of the Special Purpose Grant (B-02-SP-MI-0310)

Comments: Recommendations 1A

The EDI grant was awarded to NorthStar Community Development Corporation for the purpose of funding the implementation of the University Commons Development Plan. Essentially, the goal of the plan has not changed. The ultimate goal is the commercial and residential revitalization of the Northwest Detroit Area. The specific steps may change due to social and economic conditions but the goal will not change. It does matter how the funds were spent. NorthStar accounts for each project separately. Each project will ultimately be its own entity if is a development project and therefore proper accounting is paramount. For in house projects, (Media Center) proper cost accounting is necessary under GAAP.

During the grant period under review, some priorities changed or better stated, the timetable for certain items to be developed changed. Thus the activities and budget was amended. These changes, all consistent with the development plan, were as follows:

	Budget	Revisions	Budget
Community House Rehab	\$ 95,000.00	\$ (80,025.11)	\$ 14,974.89
University Grove Predevelopment Costs	45,000.00	(26,556.00)	18,444.00
Administration	150,000.00	(1,815.80)	148,184.20
Media Center Rehab Costs	60,000.00	12,496.91	72,496.91
Pilgrim Park Homes (lots for 11 single family homes)		46,700.00	46,700.00
Harmony Park Homes (lots for 45 single family affordable homes)		49,200.00	49,200.00
	<u>\$ 350,000.00</u>	<u>\$ -</u>	<u>\$ 350,000.00</u>

NorthStar's acknowledges that the above changes in the specifics of the plan should have been communicated to HUD. Typically, this communication is a request for a budget amendment. And, since these costs are consistent with the purpose of the grant(the implementation of the University Commons Development Plan), these costs would ordinarily be allowed and NorthStar would be allowed to continue to implement the development plan, leverage these dollars and enhance and revitalize this much needed area.

Comment 1

This clearly was an administrative error by NorthStar and in our opinion not a misuse of funds but a lack of timely reporting of changes to the plan. This plan is a living document and thus, changes are a fact of life. Due to Detroit's budget crisis resulting in police reductions and other staff reductions throughout the City government, Northstar feels that the most effective and efficient use of development funds was to increase housing in the above mentioned areas. This is consistent with the development plan and the general purpose of The Department of Housing and Urban Development. The police mini-station that had been proposed was not financially prudent given the environmental conditions.

Again, NorthStar acknowledges that prior approval of these changes was the appropriate action. Reimbursement of these funds cripples NorthStar and thwarts the much needed development in its service area. NorthStar will implement policies and procedures that address this problem. This will not happen again.

The costs of \$14,974.89 represents costs that were paid to maintain title of the building. These costs were paid outside of the grant period and represent reimbursed costs to NorthStar. Again, reimbursement would cripple NorthStar and prevent much needed development. The rehab of the building continues to be a goal of NorthStar's. We will study what alternative needs can be satisfied in that area and proceed accordingly.

Comments: Recommendations 1B

Your report indicates that \$12,120 of expenditures was not supported by invoices. Our records show that we provided invoices to you of \$10,620, omitting the tax credit application fee of \$1,500. NorthStar is submitting the following invoices for review:

Vendor	Check No.	Amount
Community Research Group	12828	4,500.00
First Title Corporation	13064	4,400.00
Juanita Wade	13068	470.00
The Envirolytic Group	14338	<u>1,250.00</u>
		<u>10,620.00</u>
MSHDA	14212	* 1,500.00

* to follow, copy of invoice to come from MI State Housing Finance Authority

Comments: Recommendations 1C

NorthStar will implement procedures and controls to ensure that timely submission of budget amendments are done properly and in accordance with HUD guidelines. Further, NorthStar will implement procedures that ensure that funds are used in accordance with approved budgets and amendments. See comments to recommendation 1A.

Comments: Recommendations 1D

It is true that NorthStar received Block Grant and Home Funds but it is policy to not double dip and charge the same expenses to different grants. Grant accounting under GAAP requires that grant revenues equal grant expenses. In other words, the financial statements will show no profit or loss from grant activities. In your report you indicate that you reviewed our audited financials and you also received trial balances from us. I am positive that it shows substantial losses. This would indicate that there are not enough revenues to support expenses. We have very little unrestricted revenue. Therefore, if we were double dipping, expenses would be less than revenues and thus profit. We have made a conscious effort not to charge expenses to more than one grant. We will review all grant reports to assure that this did not happen.

As it relates to the \$85,000 public facility grant, you will find that this grant was awarded but not received during your audit period. The work has just begun and the improvements are different than those activities charged to your grant. As a matter of fact, work related to this grant and an additional grant is scheduled to begin early 2006.

Comments: Recommendation 2A

NorthStar intends to adhere to these recommendations and record covenants on the land titles assuring nondiscrimination based on race, color, national origin, or handicap and record liens for NorthStar's Center, Harmony Park, Pilgrim Park Homes and University Grove Homes.

Comments: Recommendation 2B

Same as 2A.

OIG Evaluation of Auditee Comments

Comment 1 NorthStar provided supporting documentation for \$10,150 in unsupported disbursements relating to University Grove. Therefore, we adjusted our report by reducing the amount of Grant funds NorthStar lacked supporting documentation to \$1,970. We reduced the unsupported disbursements in acquisition costs for the property located at 15710 Dexter Avenue to \$470. We did not remove the \$470 in acquisition costs for the property located at 15710 Dexter Avenue since NorthStar only provided a hand written note as supporting documentation. Further, NorthStar did not provide documentation for the \$1,500 for a tax credit application to the Michigan State Housing Development Authority. We also adjusted the recommendation that HUD's director of congressional grants require NorthStar to provide documentation to support unsupported expenses cited in finding 1 by reducing the amount to \$1,970.

The supporting documentation NorthStar provided was for environmental assessment, market study, and closing costs for University Grove properties. Therefore, we adjusted our report by increasing the amount in which NorthStar did not secure HUD's interest in Grant funds used to acquire, or aid in the acquisition of, and/or rehabilitate real property to \$184,871. We increased the amount relating to the University Grove properties to \$16,474 and added environmental assessment, market study, and closing costs. We also adjusted the recommendation that NorthStar's recording of covenants and liens should help ensure that NorthStar protects HUD's interest by increasing the amount to \$184,871.

Appendix C

FEDERAL REQUIREMENTS

NorthStar's grant agreement with HUD, article I, section A, states grant funds will be used for activities described in the application. Section B of the grant agreement, states the grants funds must be made available in accordance with 24 CFR [*Code of Federal Regulations*] Parts 1 and 8. Section E of article I states NorthStar will comply with 24 CFR [*Code of Federal Regulations*] Part 84.

Section 7 of NorthStar's application, dated May 7, 2002, includes a project description stating NorthStar would use the \$350,000 Grant for its Varsity Park Development Plan, consisting of two housing developments called University Grove and Pilgrim Village Homes; Community House, a mini substation for the Detroit Police Department; Titan Pointe, a housing development; Revitalife, a scattered-site housing program; and administrative expenses. However, HUD approved an amended budget for the \$350,000 Grant in October 2003. NorthStar's amended budget included the following expenses: \$150,000 for administration; \$95,000 for Community House rehabilitation, \$60,000 for the Center rehabilitation, and \$45,000 for University Grove predevelopment.

According to 24 CFR [*Code of Federal Regulations*] 1.5(a)(2), in the case of real property, structures, improvements thereon, or interests therein, acquired through a program of federal financial assistance, the instrument effecting any disposition by the recipient of such real property, structures or improvements thereon, or interests therein shall contain a covenant running with the land assuring nondiscrimination based on race, color, or national origin for the period during which the real property is used for a purpose for which the federal financial assistance is extended or for another purpose involving the provision of similar services or benefits.

According to 24 CFR [*Code of Federal Regulations*] 8.50(c)(2), when no transfer of property is involved but property is purchased or improved with federal financial assistance, the recipient shall agree to include a covenant in the instrument effecting or recording any later transfer of the property for the period during which it retains ownership or possession of the property to assure nondiscrimination based on a handicap.

HUD Directive 84.32 and 24 CFR [*Code of Federal Regulations*] 84.32(a) state title to the real property shall vest in the recipient as long as the recipient uses the real property for its authorized purpose and does not encumber the real property without HUD's approval. Section 84.32(c) states when the real property is no longer needed for the authorized purpose or cannot be used in other HUD-approved federally sponsored projects or programs with purposes consistent with the authorized purpose of the original project, the recipient shall request disposition instructions from HUD. HUD shall require the recipient to do the following: (1) retain title to the real property without further obligation to the federal government after it compensates the federal government the percentage of the current fair market value of the real property attributable to the federal participation in the project, (2) sell the real property and compensate the federal government for the percentage of the current fair market value of the real property attributable to the federal participation in the project, or (3) transfer title to the real property to the federal

government or to an eligible third party and be entitled to compensation for its percentage of the current fair market value of the real property.

According to 56 *Federal Register* 16337, directive means a handbook (including a change or supplement), notice, interim notice, special directive, and any other issuance that the department may classify as a directive.

Office of Management and Budget Circular A-122 states fines and penalties resulting from violations of, or failure of an organization to comply with federal, state, and local laws and regulations are unallowable.

North Star's president certified in Standard Form 424D, Assurances – Construction Programs, section 3, that NorthStar would record the federal interest in the title of real property in accordance with awarding agency directives and would include a covenant in the title of real property acquired in whole or in part with federal assistance to assure nondiscrimination during the useful life of the project.