

Audit Related Memorandum

Issued: October 17, 1995

No: 96-BO-212-1802

TO: Jeanne McHallam, Director, Multifamily Division, Office of Housing,  
Massachusetts State Office

FROM: William D. Hartnett, District Inspector General, Office of Audit

SUBJECT: Charlesview Apartments  
Multifamily Mortgage Operations  
Allston, Massachusetts

### Introduction

We conducted an audit of Charlesview Apartments, a 221 (d)(3) project located in Allston, Massachusetts. Audit work was performed between June, 1995 and August, 1995 and covered the period January 1, 1994 through May 1995. We conducted the review in accordance with generally accepted auditing standards.

Our objectives were to assess the projects physical condition and whether the current rental structure could support repair estimates. To accomplish our objective we reviewed physical inspection reports and financial reports for the last three fiscal years. We also projected increased revenues and subsidy requirements for a possible rent increase and analyzed the impact of the rent increase would have on current tenants at Charlesview.

### Summary

The project has not raised rents since 1991 and, therefore, is not generating sufficient income for repairs. The project currently needs over \$3 million for repairs.

The Project is not generating sufficient revenue to properly maintain the project. The prior Management Agent kept rents artificially low by not requesting rent increases. The reduced rental income precluded management from performing critical project repairs. Projects rents are now substantially below the Fair Market Rents (FMR). Further, these low rents have caused substantial Section 8 resources, which could supply funds for needed repairs, to be under utilized. Over \$4 million in Section 8 fund authority will lapse within the next three years.

Our analysis showed that a significant rental increase was possible since

the majority of tenants would receive additional Section 8 subsidy to offset the increase. Working with you and your staff we supplied data which enabled the auditee to request and you to quickly approve a substantial rent increase to address the repair problems.

Since you are taking action to address the repair problems which will lower HUD's insurance risk, no audit recommendation is necessary. The attached finding details our analysis and provides data for your staff's use.

## Background

Charlesview Apartments (023-55128) is a 221 (d) (3) project, consisting of 10 buildings containing 210 apartments and four commercial units, located at Allston, Massachusetts. The project is owned and operated by Charlesview Inc., a consortium of three local churches. Josephine Fiorentino, President of Charlesview Inc., was the Chairman of the Churches Board of Directors.

Until December of 1994, the project was managed by Carter Realty of Allston. The Counsel elected to terminate the prior Management Agent. Claremont Management Corporation replaced Carter Realty Inc. in January of 1995. Claremont Management has submitted a rent increase to HUD and is currently processing tenant comments.

We appreciate the cooperation and assistance of the Claremont Management Corporation and you and your staff in conducting this review.

Please furnish us copies of any correspondence related to this review. A copy of this memorandum has been provided to Charlesview Inc. Should your staff have any questions, please contact our office at (617) 565-5259.

## Attachment

### The Project Needs More Revenue

Charlesview is not generating sufficient revenue to fund needed repairs. The project's estimated repair requirements have now increased to over \$3 million. Rents have not been increased since 1991 and are now well below Fair Market Rents (FMRs). Further, because of these low rents, Section 8 subsidies have been under-utilized. As a result, Section 8 reserves have increased to over \$4 million and are in danger of being lost when the HAP contracts expire within the next three years.

Since 1991, the Board allowed the prior manager to follow a philosophy of keeping rents artificially low even though the majority of tenants qualified for Section 8 assistance. The artificially low rents did not generate sufficient income to keep up with project repair requirements. The project now needs in excess of \$3 million in repairs.

Rents charged for Charlesview apartments are well below Fair Market Rents in the local area. Charlesview rents range between \$229 to \$680 below Fair Market Rents for the Boston area.

BR Size	Project Rents	FMRs	Difference
1	\$414	\$ 643	\$ 22
2	\$445	\$ 804	\$359
3	\$479	\$1,005	\$526
4	\$501	\$1,181	\$680

While the project continued to pay expenses, debt service requirements and replacement reserve deposits, the rents were not sufficient to generate enough funds to pay for major repairs.

Fiscal Year	1992	1993	1994
Revenues	\$1,147,626	\$1,194,036	\$1,209,483
Expenditures	\$1,119,252	\$1,140,634	\$1,151,693
Cash throw-off	\$ 28,374	\$ 53,402	\$ 57,790

Due to lack of cash flow, the project delayed critical repairs. Physical inspections demonstrate a steady decline in the project's physical condition:

Inspection Date	Repairs Required
June 11, 1990	\$ 290,000
April 16, 1991	\$ 374,550
April 14, 1995	\$1,774,903
August 22, 1994	\$1,912,665
July 11, 1995	\$3,053,568

The Regulatory Agreement requires the owners to keep the project in good repair and condition. It is clear that the Regulatory Agreement is not being followed and the project is deteriorating. This deterioration jeopardizes HUD's interest and creates an unnecessary risk to the Insurance Fund.

The project has two Section 8 Housing Assistance Program (HAP) contracts covering 200 units. Contract MA06000036 is for 158 units and expires on October 31, 1996 and Contract MA06L000167 for 42 units will expire on May 31, 1998. These two contracts can potentially provide the project \$1,054,580 annually for Section 8 assistance. As of May, 1995, the project was drawing down about \$287,000 per year.

Many tenants who qualified for Section 8 did not require subsidy because their income is sufficient to pay the project's artificially low contract rents. As of May, 1995, 47 of the 89 tenants not receiving Section 8 assistance were paying less than 20 percent of their income for rent. For those qualified tenants receiving Section 8 subsidy, the low rents reduced the amount of subsidy HUD needed to pay. As a result, only 116 of the 200 Section 8 units were being used and Section 8 project reserves for these contracts grew to the following amounts as of July 31, 1995:

MA00036 - \$2,922,848  
 MA00167 - \$1,064,168

Upon the expiration of these HAP contracts, these funds cannot be used for project expenses or repairs and either sit idle or are returned to the Treasury. Currently, the only available use of these funds is to supplement tenant-rent payments.

The rents need to be increased to a realistic level to generate funds for critical repairs. The higher rents will increase the number of tenants who receive Section 8, and for those tenants already receiving Section 8, will increase the subsidy HUD pays on their behalf, therefore, generating additional project income for repairs.

As an example, we calculated the effect of a 40 percent across the board rent increase. Such a rent increase would still leave Charlesview Rents 10 - 40 percent below the Fair Market Rents in the immediate area while generating significant additional revenue.

	Monthly Tenant Rents	Monthly Subsidy Rents	Annual Total *
Present Rents	\$69,667	\$23,905	\$1,122,864
Rents+40% *	\$91,446	\$39,555	\$1,572,012
Increases	\$21,779	\$15,650	\$ 449,148

\* Calculated by auditor

These additional funds could be earmarked for project repairs.

We found that the impact of these rent increases on the majority of the current tenants would not be severe. The majority of tenants would be protected by Section 8 subsidy. We found that:

- o 116 of the tenants now on Section 8 would be protected from the rent increase by an increase in HUD's Section 8 subsidy on their behalf.
- o 29 tenants not now receiving Section 8 subsidies would require subsidies to keep their rents at 30 percent of income. Of these 29 tenants, 16 were eligible for Section 8 subsidies and 2 were not eligible when they moved in. In 11 cases, available records were not sufficient to determine if the tenant was eligible for Section 8 subsidy.
- o 60 tenants were not on subsidy and would not require subsidy to remain at Charlesview. Their rent burden, currently between 9 to 27 percent of monthly income, would increase to 12 to 30 percent of monthly income. Twenty-one of these tenants were market rate tenants with an average income of \$51,510 who have resided at Charlesview for an average 18 years. These tenants paid a 10 percent premium over contract rents. If these tenants should elect to move out, occupancy should not be a problem as there is a waiting list of 178 families ready to replace them. Should additional Section 8 eligible people move in, there would also be an increase the Section 8 funds being drawn.

\* \* \* \* \*

We met and discussed this matter with HUD Massachusetts State Officials who agreed with our analysis. During August, 1995, they instructed the Management Agent to process a significant rent increase. On August 31, 1995, the Management Agent issued a notice to tenants of a proposed 40 percent rent increase to be submitted to HUD which provided for a 30-day period for tenants to review materials and submit comments. On October 2, 1995, the "Request for Rental Increase", which has a target date of November 3, 1995 to approve, adjust, or reject the proposal, was submitted to HUD and they are currently reviewing it.

Based upon the results of our audit, we are not making any specific recommendations. The Massachusetts State Office is taking the appropriate action to provide the cash flow necessary to restore and maintain the project's physical condition and protect HUD's interest.

