



Issue Date	August 5, 2009
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Audit Report Number	2009-KC-1009
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TO: Brenda L. Waters, Acting Hub Director, Kansas City Multifamily Hub, 7AHMA

//signed//

FROM: Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

SUBJECT: Milestone Management Systems Inc.'s Management Controls for Managing Multifamily Properties Were Not Adequate

HIGHLIGHTS

What We Audited and Why

We audited Milestone Management Services, Inc. (Milestone), of Topeka, Kansas, in response to a request from the U.S. Department of Housing and Urban Development's (HUD) Office of Multifamily Housing in Kansas City, Kansas. HUD was concerned that Milestone had not complied with cash management requirements.

Our audit objective was to determine whether Milestone complied with HUD's cash management requirements for management agents.

What We Found

Milestone's management controls were not adequate in three respects. Milestone did not (1) adequately segregate duties of on-site staff or provide proper oversight of these employees, (2) have a system for tracking significant rehabilitation and related costs for individual units, or (3) practice proper budgetary controls. In addition, Milestone did not provide its properties with adequate fidelity bond coverage, and it overpaid itself management fees.

What We Recommend

We recommend that HUD ensure that Milestone/property owners implement an adequate system of management controls and provide technical assistance and guidance as needed. We also recommend that HUD require Milestone/property owners to implement procedures to periodically assess the adequacy of fidelity bond coverage and adjust the coverage for each property when needed. Further, we recommend that HUD ensure that Milestone/property owners use a reliable process to calculate and pay management fees and that Milestone immediately repays overpaid management fees to the overcharged properties. Lastly, we recommend that HUD take appropriate administrative actions against Milestone/property owners if Milestone is unable or unwilling to comply with HUD requirements.

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 the draft report to Milestone on June 10, 2009, and requested a response by July 29, 2009. Milestone provided comments on July 28, 2009. It generally agreed with our findings and recommendations.

The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVE

Milestone Management Services Inc. (Milestone), is a property management company operating out of Topeka, Kansas. Milestone was incorporated on February 6, 1989, and began managing U.S. Department of Housing and Urban Development (HUD)-related multifamily properties in the same year. During our audit period, Milestone managed seven multifamily properties located in Kansas, Missouri, and Illinois. Five of the properties were housing cooperatives, and two were not.

Milestone managed HUD-insured and/or HUD-assisted properties governed by the following sections of the National Housing Act, as amended:

- Section 213 – Mortgage Insurance for Cooperative Housing
- Section 221(d)(3) and (4) – Mortgage Insurance for Rental and Cooperative Housing
- Section 236 – Subsidized Mortgages/Interest Reduction Programs

Under these sections of the National Housing Act, property owners enter into regulatory agreements with HUD. The regulatory agreements contain certain provisions, including but not limited to establishing and maintaining property reserve accounts, collecting rents, and performing property maintenance.

Property owners are ultimately responsible for ensuring that the properties are operated in accordance with the regulatory agreement and applicable HUD handbooks. However, property owners may contract with a management agent, such as Milestone, to carry out the day-to-day management of the property. As the management agent, Milestone signs a HUD certification that it agrees to comply with the property's regulatory agreement as well as other HUD requirements.

Milestone and the property owners also enter into a management agreement between themselves, which details the expectations and responsibilities of the management agent. One of Milestone's key responsibilities as the management agent is the oversight and supervision of personnel working on site at the properties. These on-site employees, such as the office and maintenance personnel, are employees of the property, not employees of Milestone.

Our audit objective was to determine whether Milestone complied with HUD's cash management requirements for management agents.

RESULTS OF AUDIT

Finding 1: Milestone's Management Controls Were Not Adequate

Milestone's management controls were not adequate. This deficiency occurred because Milestone did not fully understand the importance of a strong system of management controls. As a result, HUD and property owners could not be assured that Milestone's efforts reasonably protected its properties' funds from fraud, waste, and abuse.

Milestone's management controls were not adequate in three respects. Milestone did not (1) adequately segregate duties of on-site staff or provide proper oversight of these employees, (2) have a system for tracking significant rehabilitation and related costs for individual units, or (3) practice proper budgetary controls.

No Segregation of Duties with Limited Oversight of Property Staff

Milestone did not provide for adequate segregation of duties for on-site staff, nor did it provide acceptable oversight of these employees. HUD's handbook governing financial operations and accounting procedures for insured multifamily properties contains detailed requirements for segregation of duties involving financial transactions. Further, as the management agent, Milestone was responsible for supervising on-site property employees to properly maintain and operate the property.

Milestone allowed on-site property managers to control most cash income processes without properly overseeing or validating their work. On-site managers collected tenant rents, posted rent payments to tenant accounts maintained in a separate set of books and records at the properties, and prepared and made bank deposits. Further, Milestone's accounting system was not integrated with the various properties it managed, so it relied on bank deposit information and month-end rent collection records prepared by the on-site property managers. Based on the information from the managers, Milestone posted only total rents collected to its own set of accounting records for each property but did not independently verify the validity of the information. In addition, it made on-site property managers solely responsible for following up with tenants regarding late or unpaid rent.

In December 2006, Milestone learned that one on-site manager had stolen tenant rents for more than three years. The property's bank had notified Milestone that the manager had made suspicious financial transactions with money orders made out to the property. Milestone conducted a financial review and confirmed the long-term theft. Milestone had inappropriately allowed the employee to control all aspects of

the rent collection, deposits, recording, and late/unpaid rent follow-up process. The employee was able to manipulate the tenant records and accounting information and report false information to Milestone to hide the theft.

For another property, Milestone allowed an assistant maintenance supervisor to approve and submit property invoices for rehabilitation and maintenance costs without oversight. It paid the invoices without verifying the legitimacy of the invoices or that the described work had been completed. Instead, it relied on the on-site employee's approval. Milestone told us that it believed that an invoice containing the initials of the on-site manager or the assistant maintenance supervisor was sufficient to validate a property expense. However, Milestone later learned from other property employees, and subsequently confirmed, that the assistant maintenance supervisor had submitted a number of false invoices. Milestone paid the invoices because it did not recognize that the invoices were false. The scheme occurred because neither Milestone nor the on-site property manager had provided adequate oversight.

No Tracking System for Costs of Substantial Rehabilitation Work

Milestone did not have a system for tracking or following up on significant rehabilitation work performed on individual units. According to the management agreements between Milestone and the properties it managed, Milestone was to maintain a comprehensive system of records, books, and accounts. It also signed HUD certifications that it agreed to ensure that all expenses of the properties were reasonable and necessary.

During the audit period, Milestone managed renovations of a number of units at its largest property. Although the property had in excess of 500 units, Milestone could not provide a detailed plan or schedule identifying what units were to be rehabilitated, by when, or at what cost for each unit. In addition, Milestone did not conduct adequate on-site verifications of completed rehabilitation work. It visited the property but did not conduct detailed inspections of the units. Further, it did not track renovation costs per unit. Therefore, it could not identify questionable costs charged for a unit, such as duplicated or unnecessary costs, nor could it compare the costs charged to the actual work completed to ensure that the costs were valid.

The lack of a tracking system allowed the assistant maintenance supervisor to submit multiple invoices for payment for the same goods and services for the same unit. Milestone then paid fraudulent invoices that contained identical items for the same unit as many as five times. Milestone told us that the software system it used to generate payments identified duplicate invoices based only on the invoice number and the system did not have the ability to track or sort expenses by unit.

Lack of Budgetary Controls

Milestone did not practice proper budgetary controls. Management agreements between Milestone and the properties required Milestone to prepare monthly financial reports, including a comparison of monthly income and expenses to the budget. Milestone generally provided monthly accounting and budget variance reports to owners and board members and discussed the reports at board meetings. However, it did not use the reports as a tool to help manage the properties, particularly when income was noticeably less than expected or expenses were significantly higher than expected.

In addition, Milestone did not always make required monthly deposits to properties' general operating reserve accounts, and it exceeded withdrawal limits without obtaining HUD's approval. The purpose of the general operating reserve fund is to provide a measure of financial stability and to meet unforeseen financial obligations of the property. The properties' regulatory agreements require the owner (or its management agent) to make monthly deposits to the operating reserve account equal to a certain percentage of rent collections for that month. In addition, property owners and designated agents are not permitted to make withdrawals from the general operating reserve in excess of a certain limit without HUD's approval.

For one property, the independent auditor noted that Milestone did not make any of the required deposits to the general operating reserve account for fiscal year 2007. Milestone also exceeded withdrawal limits for this property without first obtaining HUD's approval. Milestone told us that it did not seek HUD's approval when it exceeded withdrawal limits because the property needed the funds immediately to pay its monthly operating expenses. However, if Milestone had used proper budgetary controls, it should have been able to plan for required HUD approvals.

For another property, in fiscal year 2008, Milestone did not make the required monthly deposits but, instead, arbitrarily made deposits throughout the year to fulfill the requirement. Prior HUD reviews for fiscal years ending 1999, 2000, and 2001 also revealed problems with Milestone's not funding properties' general operating reserve accounts and making unauthorized withdrawals.

Importance of Management Controls Not Fully Understood

Milestone did not understand that a strong system of management controls is necessary to safeguard its properties' assets and provide for accurate books and records. Instead, it relied on limited site visits to ensure that its on-site employees properly managed the properties.

Property Assets Susceptible to Errors, Waste, and Fraud

HUD and property owners could not be assured that Milestone's efforts reasonably protected property funds or met budgetary control and financial stability requirements. This problem is illustrated by the on-site employee thefts at two of Milestone's properties. Both thefts occurred over periods lasting at least three years. Milestone estimated property losses at more than \$300,000. In addition, its independent auditor raised substantial doubt about one of the property's ability to continue as a going concern. The auditor was mainly concerned about high vacancy rates but the employee theft of about \$200,000 also contributed to the property having difficulty meeting daily operations costs. That property continued to experience severe cash flow problems and could place HUD at risk for the \$11 million balance on its insured mortgage. If Milestone had practiced proper management controls, it should have been able to either prevent the employee thefts or detect and end them before the properties experienced significant losses.

Conclusion

Milestone's management control efforts did not provide reasonable assurance that property funds were protected from fraud, waste, and abuse. HUD and property owners relied on the management agent to successfully manage properties and to do so in accordance with HUD rules and regulations. However, Milestone did not understand the importance of segregation of duties, sufficient management oversight, tracking of property expenditures, and proper budgetary controls. If Milestone had practiced proper management controls, it could have better protected property assets.

Further, the above deficiencies along with those in findings 2 and 3 detailed later in this report, describe significant and repeated breaches of commitments to HUD and violations of HUD requirements. These deficiencies rise to a level to which HUD needs to consider whether Milestone can immediately improve its operations to fully comply with HUD requirements, or whether HUD should no longer allow Milestone to manage HUD properties.

Recommendations

We recommend that the Director, Office of Multifamily Housing, Kansas City, Kansas,

- 1A. Ensure that Milestone/property owners implement an adequate system of management controls.

- 1B. Provide technical assistance and guidance to Milestone as needed.
- 1C. Take appropriate administrative actions against Milestone/property owners if Milestone is unable or unwilling to comply with HUD requirements.

Finding 2: Milestone Did Not Provide Properties with Adequate Fidelity Bond Coverage

Milestone did not provide the properties with adequate fidelity bond coverage. This deficiency occurred because Milestone did not periodically assess whether fidelity bond coverage was within acceptable limits. As a result, multifamily properties were placed at unnecessary risk of loss.

Inadequate Fidelity Bond Coverage for Two Properties

Milestone did not provide two properties with adequate fidelity bond coverage during the audit period. A fidelity bond is an insurance policy that protects property owners against financial loss resulting from dishonest acts of its employees. HUD regulations and management certifications signed by Milestone require property owners or their designated management agents to obtain a fidelity bond in the amount at least equal to potential rent collections for two months.

One property had fidelity bond coverage of \$100,000 in effect at the time of the audit. However, the potential rent collections for two months were nearly \$170,000. We notified Milestone of this deficiency, and it increased the property's fidelity bond coverage to \$200,000, effective retroactively to September 2008.

Another property did not have adequate coverage for 2007 and most of 2008. The property's rent revenue increased substantially in 2007, primarily due to an increase in rents. However, Milestone did not increase the property's fidelity bond coverage to an adequate level until September 2008. As a result, the property was underinsured by approximately \$150,000 for the 21-month period.

Adequacy of Coverage Not Periodically Assessed

Milestone did not periodically assess whether fidelity bond coverage was within acceptable limits. The fidelity bond coverage requirement is based on a variable (potential rent collections) that may change over time, and, therefore, the acceptable amount of coverage may also change. Milestone and property owners were jointly responsible for reasonably assessing coverage and ensuring that the properties' fidelity bond policies were sufficient.

Multifamily Properties Placed at Unnecessary Risk of Loss

Two multifamily properties were unnecessarily vulnerable to risk of loss. Milestone and property owners were responsible for safeguarding property assets

and mitigating potential losses. Maintaining adequate fidelity bond coverage to cover employee dishonesty was a way to protect HUD and property owners from losses, and Milestone and the owners should have taken the steps necessary to secure proper coverage.

Recommendation

We recommend that the Director, Office of Multifamily Housing, Kansas City, Kansas,

- 2A. Require Milestone/property owners to implement procedures to periodically assess the adequacy of fidelity bond coverage and to adjust the coverage for each property when needed.

Finding 3: Milestone Overpaid Itself Management Fees

Milestone overpaid itself management fees. This problem occurred because Milestone did not have a reliable process for calculating and paying itself management fees, nor did it provide supporting documentation to property owners. As a result, properties did not have access to all of their operating funds.

Overpaid Management Fees

Milestone overpaid itself management fees. Its monthly compensation was established by the management agreements between itself and the properties it managed. The individual management agreements identified a certain percentage of gross collections to be paid monthly to Milestone from the properties' operating account. Because Milestone was responsible for generating the payments for properties' expenses, it generated payments to itself for the management fees.

Milestone overpaid itself nearly \$6,700 for one property (property A) for the fiscal year ending September 30, 2008, and owed the property more \$600 from prior periods as of the end of our audit. HUD agreed and instructed Milestone to repay more than \$7,000 to the property in March 2009.

Milestone had a history of overpaying itself management fees. The properties' independent auditor identified such overpayments as significant deficiencies for the properties and periods indicated in the chart below.

Property name	Fiscal year ending	Management fee overpayment
Property A	September 30, 2006	\$1,128
Property B	December 31, 2007	\$2,643
Property C	June 30, 2008	\$3,186

Milestone repaid the amounts indicated in the chart above. However, HUD recently determined that Milestone overpaid itself an additional \$3,800 for property B for the same period identified in the chart. HUD instructed Milestone to repay this amount to the property in March 2009.

Milestone recently notified HUD that it disagreed with the amounts identified as overpaid and not yet repaid for properties A and B. As of this report, HUD was evaluating Milestone's disagreement with the amounts.

Unreliable Process for Calculating Management Fees

Milestone did not have a reliable process for calculating and paying itself management fees. It also had not provided supporting documentation to owners. For most properties, Milestone made two payments to itself from the properties' accounts each month. Contrary to the management agreement, the first payment was generally a flat fee paid at the beginning of the month, and the second payment was made during the middle of the month. Milestone told us that it based the second payment on estimated collections. It had not provided supporting documentation to most property owners to show how it had calculated the payments.

Properties without Access to All Funds

The properties did not have access to all of their operating funds. In addition, the overpaid management fees essentially resulted in improper loans from the properties to Milestone. Further, property owners could not readily assess whether the management fees paid to Milestone complied with the management agreements.

Recommendations

We recommend that the Director, Office of Multifamily Housing, Kansas City, Kansas,

- 3A. Ensure that Milestone/property owners use a reliable process to calculate and pay itself/themselves management fees. This process should include procedures through which Milestone would base its fees only on actual gross collections and provide detailed invoices showing monthly management fee calculations to property owners.
- 3B. Ensure that Milestone immediately repays \$7,359 to property A and \$3,866 to property B, and any additional overpaid management fees to the respective overcharged properties, unless Milestone provides adequate evidence that it had not overpaid itself.

SCOPE AND METHODOLOGY

Our review generally covered the period October 2005 through September 2008. We conducted our audit work from November 2008 to March 2009 at Milestone's office at 4900 Fairlawn Road, Topeka, Kansas.

To achieve our objective, we conducted interviews of Milestone management and staff. We also interviewed HUD staff in the Kansas City, Kansas, Office of Multifamily Housing. We evaluated a management review of Milestone that HUD conducted in 2002. We also reviewed management reviews HUD conducted in 2008 for two properties that Milestone managed.

We reviewed the property regulatory agreements, management certifications, management agreements, and applicable HUD handbooks and regulations. We also reviewed Milestone's policies and procedures. In addition, we reviewed the records of a sample of properties based on property information provided by HUD and those properties with a larger number of housing units. We tested cash receipts and/or expenditures on the following properties:

- Pin Oak Acres Apartments, Inc.
- Parade Park Homes, Inc.
- Fox Ridge Cooperative Townhouses, Inc.

To test cash receipts and expenditures, we reviewed property budgets, bank statements, check registers, payroll journals, cash receipt journals, rent rolls, invoices, and general ledgers. We also reviewed audited financial statements for four properties that Milestone managed:

- Pin Oak Acres Apartments, Inc. – fiscal year ending September 30, 2006
- Prairie Glen East Cooperative, Inc. – fiscal year ending December 31, 2007
- Parade Park Homes, Inc. – fiscal year ending December 31, 2007
- Fox Ridge Cooperative Townhouses, Inc. – fiscal year ending June 30, 2008

We reviewed the fidelity bond policies for six properties, including the four identified above as well as Wheatview Apartments and North Park Tower Cooperative. In addition, we reviewed Milestone's analysis of employee thefts that occurred at two of the properties.

We reviewed reports generated by Milestone's computerized accounting system (CYMA Accounting Software). We used the computerized data for background and informational purposes only; therefore, we performed no tests of the data.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

INTERNAL CONTROLS

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

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

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

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective: Milestone's management controls for

- Evaluating the validity of property expenses.
- Ensuring receipt and proper recording of property receivables.
- Calculating and paying management fees.
- Complying with applicable laws, regulations, and agreements.
- Preparing and evaluating property operating budgets and variance reports.

We assessed the relevant controls identified above.

A significant weakness exists if management 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 review, we believe that the following items are significant weaknesses:

- Milestone did not provide for segregation of duties or provide acceptable oversight of on-site property employees (finding 1).
- Milestone did not have a system for tracking or following up on significant rehabilitation and related costs for individual units (finding 1).
- Milestone did not practice proper budgetary controls for its properties (finding 1).

- Milestone did not periodically assess whether fidelity bond coverage was within acceptable limits (finding 2).
- Milestone did not have a reliable process for calculating and paying itself management fees (finding 3).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/
3B	\$7,359

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.

Although recommendation 3B also includes a recommendation for Milestone to repay \$3,866 in ineligible costs to the applicable property, HUD identified this amount independent of our audit. Therefore, we did not include this amount as a questioned cost.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

	1734 E. 63rd Street, Suite 101 Kansas City, MO 64110 (816) 363-3063 Fax (816) 363-3063
<u>MILESTONE MANAGEMENT SERVICES, INC.</u> Property Management Specialists	PMB 367 6021 S.W. 29th Street, Suite A Topeka, Kansas 66614-4269 (785) 862-7097 Fax (785) 862-7099
July 28, 2009	
Ronald Hosking Regional Inspection General for Audit Dept. of HUD Office of Inspector General 400 State Avenue Kansas City, KS 66101-2406	RE: Draft Audit for Milestone Management Services, Inc.
Dear Mr. Hosking:	
As a result of the June 10, 2009 draft audit report by your office which was conducted from November 2008 to present with most of its work being finished in March of 2009, but many questions and corrections or changes have gone on until this date. With that we are making our response.	
It is extremely hard for me to respond to this report since I have managed several of these properties for over 26 years and over 20 years as Milestone Management Services, Inc. Some of them I have not managed but 2 to 3 years.	
First, I would like to say that almost "all" of these findings were previously reported to HUD and owners by our office or their independent CPA. There were two incidents of fidelity bonds being too low. The first "one" worked on from an auditors report and had it in the works to increase before the OIG audit. The second fidelity bond being too low was also in the works with the property's insurance company and was completed shortly before our change in management. These were the only two items which HUD may not have been aware of previous to this audit.	
Milestone is certainly willing to make any changes necessary to fully comply with all HUD requirements. In fact, we have already taken many steps to improve our oversight as in part witnessed by enclosed memos and directions issued to site and Milestone personnel.	
We will now address three (3) of the major findings:	
Finding 1)... We agree that there was not enough oversight and segregation of duties with various key site personnel. Following the incident with the theft of money by the site manager, we of course terminated her and made many adjustments to the collection and	

Comment 1

Ref to OIG Evaluation

Auditee Comments

Comment 2

deposit systems, double check and match collections with recorded tenant payments and now also require someone other than who posts to make actual deposits (see memo of April 21, 2009). We are also making more frequent spot checks of all books and files. These procedures are for all properties. All but one of our properties now utilizes Yardi for there on site collections and tenant records.

Comment 3

Also in the incident of the assistant maintenance supervisor signing off on invoices not completed and received money back from the contractors, we terminated the employee finally after the owners originally denied his termination. Again, we relied too much on the site manager additionally signing off on these invoices. Now we double check any large invoices and implemented other procedures to safeguard this sort of theft (see June 15, 2009 memo).

We are also in the process of changing our bookkeeping system to a more advanced Yardi system which will track duplicate payments and we are making a lot more frequent spot checks of vacancies and rehabilitation units.

Milestone did prepare monthly budgets for owners and at most properties reviewed and reported line items which were over budget significantly and why they were. We will now make a practice of this report to all property owners. We will also make spot checks and verification of any of these purchases which are high.

In the past we have taken money from General Operating reserves without first obtaining HUD permission, sometimes at the express direction of the owners or Board of Directors. Most times, these were paid back and always reported to HUD by the property CPA. This will never be done again, regardless of who wants it (see In House Memo of July 20, 2008).

Also, all required deposits will be made on a monthly basis. As far as the losses were concerned, the first has been reimbursed by fidelity bond coverage and the second currently in the works of being rectified by property or Milestone fidelity bonds and Milestone's Errors and Omissions insurance.

Finding 2)... I think we have discussed the shortage in Fidelity Bond coverage's in the opening of this response. We now thoroughly review the property coverage at the time of any HUD approved increase in collections and make immediate additions to coverage if required.

Comment 4

Finding 3)... Milestone did occasionally overpay itself management fees in error throughout the years due to estimating payments on some properties. We have since discontinued this practice. (See in house memo date 07/29/08)

Ref to OIG Evaluation

Auditee Comments

Comment 5

In each instance the overpayments were always paid back by Milestone and reported to HUD and the owners by their CPA via the properties annual financial statements. There were also many years where the estimations resulted in the property owing Milestone. This had been going on for 20 years and HUD never said anything other than it needed to be paid back if we were overpaid.

As stated in this draft we are still in dispute with HUD over two (2) computations of overpayments that HUD has computed differently than the properties CPA's firm which are the figures we went by. We are in hopes these can be cleared up soon and of course if found that there is an outstanding balance it will be paid immediately.

I think we have covered all of the main areas in each of the findings. In conclusion I would like to say that putting anything we have ever done wrong over 20 years in a small draft like this certainly paints a black picture and it is certainly a shame that valued, trusted employees turn out to be unscrupulous thieves with very devious methods actually lead to this audit. Although I agree that better oversight may have prevented some of these things I think that in the big picture we have always taken care of our properties. They are all in good physical shape, they have all recently had good HUD reac inspections with scores being in the 80's and 90's. They all have good reserves as appropriate to their size with one having over \$880,000. We have worked one through a refinancing and rehabilitation after original loans were paid off. We are very near to prepaying two (2) other HUD loans, refinancing and also rehabilitating with major work to continue the good affordable housing. Another property in this group we have also managed for 20 years leaving it in very good shape, great reserves and only 9 months away from final payoff of their loan.

We feel these are good accomplishments and take pride in all our properties. We have made significant steps in improving our oversight procedures and given the chance to continue managing HUD properties we will continue to improve any aspect we can or are requested to do.

Finally I would like to say that all of the auditors from OIG were helpful, friendly and professional.

Sincerely,



Gary Osborn
Owner
Milestone Management Services, Inc.

Milestone Management Services, Inc.

6021 SW 29th Street, Suite A

PMB 367

Topeka, KS 66614

Phone 785-862-7097

Fax 785-862-7099

FAXED

Memorandum

TO: ALL PROPERTIES
FROM: MILESTONE MANAGEMENT

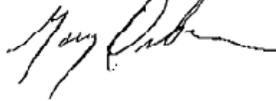
Please see attached memos to read over for your review. Please discuss the relevant topics with the appropriate departments.

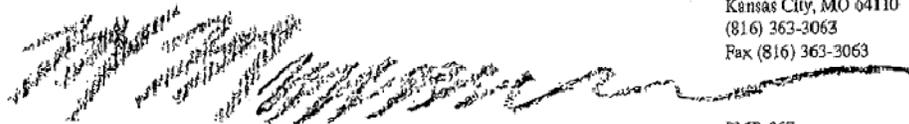
It is imperative that these procedures are implemented and followed through with on a daily basis. These are HUD Regulations and Guidelines that must be adhered to at all properties.

Again, these efforts are not a reflection on any personnel at the property, but merely a strengthening of our management oversight procedures.

Thank you.

Milestone Management Services, Inc.





MILESTONE MANAGEMENT SERVICES, INC.

Property Management Specialists

1734 E. 63rd Street, Suite 101
Kansas City, MO 64110
(816) 363-3063
Fax (816) 363-3063

PMB 367
6021 S.W. 29th Street, Suite A
Topeka, Kansas 66614-4269
(785) 862-7097
Fax (785) 862-7099

In House Memo

July 20, 2008

All Milestone Personnel:

In an effort to comply with HUD regulations and Regulatory agreements there are several things we have to change or correct as follows:

- 1)...No money shall be released from any HUD property Residual Receipts, or GOR accounts without proper HUD authorization papers regardless of management or owners authorization.
- 2)...Henceforth all Management checks for each property shall be computed per month and not estimated to prevent overpayment to Milestone.
- 3)...Finally all management checks due for the twelfth (12th) month of each year will be thoroughly scrutinized and adjusted as needed to ensure that no overpayment of management fees occurs.

These efforts are not a reflection on any personnel in our office, but merely a strengthening of our management oversight procedures.

Thank you for your cooperation.

Milestone Management Services, Inc.

Gary Osborn
Property Manager



MILESTONE MANAGEMENT SERVICES, INC.
Property Management Specialists

1734 E. 63rd Street, Suite 101
Kansas City, MO 64110
(816) 363-3063
Fax (816) 363-3063

PMB 367
6021 S.W. 29th Street, Suite A
Topeka, Kansas 66614-4269
(785) 862-7097
Fax (785) 862-7099

Memo

May 12, 2009

All Site Managers and Maintenance Supervisors:

In an effort to verify existing monthly vacancies as reported on the monthly financial reports we are now asking that copies of those vacancy report pages be copied and reviewed by any assistant managers, and maintenance supervisors.

After review, we ask that each person reviewing these forms please initial same and immediately fax to our management office.

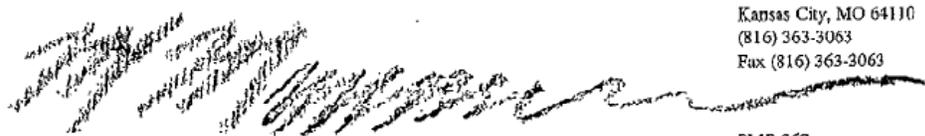
In addition, any site visits from management personnel will require random inspections of some or all vacant units as listed.

These efforts are not a reflection on any personnel at the property, but merely a strengthening of our management oversight procedures.

Thank you for your cooperation.

Milestone Management Services, Inc.

Gary Osborn
Property Manager



1734 E. 63rd Street, Suite 101
Kansas City, MO 64110
(816) 363-3063
Fax (816) 363-3063

MILESTONE MANAGEMENT SERVICES, INC.

Property Management Specialists

PMB 367
6021 S.W. 29th Street, Suite A
Topeka, Kansas 66614-4269
(785) 862-7097
Fax (785) 862-7099

Memo

June 15, 2009

All Site Managers and Maintenance Supervisors:

In an effort to verify all unit rehabilitation charges, non-charges, and contractor charges for each unit we are asking that the following procedures be followed in the future:

- 1)...Each Rehab unit shall have the required move out inspection sheet filled out by the person doing the inspection, signed and dated as required by both parties.
- 2)...Items found to need replacement or repair will be placed on work orders and signed off on the same as a regular work order when completed.
- 3)...All properties will use a similar make ready chargeable and non chargeable sheet as utilized by Fox Ridge Cooperative (as included). These sheets may be available to produce on Yardi or any other computer system your office may have.
- 4)...Particular emphasis must be placed on all contracted work including dates, Contractor, and total costs.
- 5)...Each copy of this report must be signed on the "Prepared by" line, but we also want each employee who has done any work in this Rehab unit to initial the sheet.

These efforts are not a reflection on any personnel at the property, but merely a strengthening of our management oversight procedures.

Thank you for your cooperation.

Milestone Management Services, Inc.


Gary Osborn
Property Manager

Ref to OIG Evaluation

Auditee Comments

MAKE-READY CHARGEABLE

NAME:
ADDRESS:
LABOR RATE: \$20.00 PER HOUR

Name	date	room	work required	time	materials used	labor	material	controls
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Total hours chargeable:	0	TOTALS:	\$0.00	\$0.00	\$0.00
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Prepared By: _____ Date: _____

TOTAL MATERIALS AND LABOR: \$0.00

COPY

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Ref to OIG Evaluation

Auditee Comments

MAKE-READY NON-CHARGEABLE

NAME:
ADDRESS:
LABOR RATE: \$0.00 PER HOUR

Name	date	room	work required	hrs	materials used	labor	material	contracted
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Total hours non-chargeable: 0 TOTALS: \$0.00 \$0.00 \$0.00

Prepared By _____ Date _____ TOTAL MATERIALS AND LABOR: \$0.00

2007

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Ref to OIG Evaluation

Auditee Comments

FOX RIDGE COOPERATIVE TOWNHOUSES, INC.
MAKE-READY CHARGEABLE

NAME:
ADDRESS:
LABOR RATE: \$20.00 PER HOUR

Name	date	room	work required	hrs	materials used	labor	material	contracted
ctd	6/25	unit	clean unit, clean windows & trucks	0	- clean unit \$215.00; clean oil windows & trucks \$120.00	\$0.00	\$0.00	\$335.00
ctd	6/25	unit	paint unit walls	0	- paint outside unit \$485.00; 6 gallons of paint; 1 gallon stain paint \$23.62	\$0.00	\$112.42	\$485.00
ctd	6/26	unit	clean & deodorize carpet, removed rust stain in bedroom	0	Case's Carpet Cleaning, clean carpet \$90.00, remove stain \$10.00	\$0.00	\$0.00	\$100.00
Joni	7/8	#1, #2, #3 bdms	#1, #2, #3 bdms - replace broken mini-blinds; #3 bdrm - replace burnt out light bulb	0.75	E56, 2-M34b, M33b	\$15.00	\$54.89	\$0.00
Bob	7/8	kit	replace 4 burner out light bulbs in ceiling fan, replace 3 small drip pans & rings, replace broken mini-blinds	1	4 - E16, 3 - E12, 3 - E10, M34b	\$20.00	\$31.90	\$0.00
Randy	7/8	rm, #1 bdrm, kit	rm - replace torn s/door screen, #1 bdrm - replace both torn screens, replace cracked s/window	1	screen, glass	\$20.00	\$25.97	\$0.00
Aaron	7/8	FB	replace 2 missing light bulbs	0	2 - E56	\$0.00	\$2.00	\$0.00
Bob	7/9	bson	replace broken outside globe & light bulb	0.25	E46, E50	\$5.00	\$5.27	\$0.00
Total hours chargeable:				3		TOTALS: \$60.00	\$231.25	\$920.00

Prepared By _____ Date _____

TOTAL MATERIALS AND LABOR: \$1,212.25

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OIG Evaluation of Auditee Comments

- Comment 1** As noted in the report, HUD asked that we review Milestone because HUD was concerned that Milestone had not complied with cash management requirements. HUD also told us of Milestone's past noncompliance with HUD requirements and of the two instances of property employees involved with stolen rents and false invoices. HUD's experience with Milestone led it to request that our office conduct a review of Milestone's cash management practices and controls.
- Comment 2** Milestone's written response to the report did not contain the referenced April 21, 2009, memorandum; however, Milestone provided the memorandum to us during the audit. The memorandum discussed Milestone's policy to not allow the employee that collected and recorded rents, and prepared and recorded bank deposits, to also take the cash deposit to the bank. We do not believe that this procedure sufficiently addressed our segregation of duties concern identified in finding 1. The memorandum continued to allow the same employee access and responsibility for collecting rents, recording rents received, and preparing and recording each bank deposit. Allowing one employee to perform these duties is not adequate segregation of duties because it could allow an employee to manipulate the records and misappropriate property income. Milestone needs to adequately address this issue and present evidence of acceptable improvements to HUD.
- Comment 3** Although the June 15, 2009, memorandum had merit, it was addressed to on-site property managers and maintenance supervisors. It did not address how Milestone staff would use the information to prevent duplicate invoice payments or other misappropriation of property assets. Milestone needs to provide more detailed information to HUD regarding how Milestone staff will use the information to protect property assets.
- Comment 4** The July 2008, memorandum was an appropriate notice to Milestone staff; however, during our audit we identified two instances in which Milestone did not follow the written procedure after the memorandum date. As explained in finding 3, staff did not follow the policy for one property in August and September 2008, which was immediately following the memorandum date. Milestone needs to reiterate the policy to its staff and provide evidence to HUD that it is following the policy.
- Comment 5** Our report did not address Milestone's actions for the past 20 years. As explained in the scope and methodology section of this report, our review generally covered the period October 2005 through September 2008. We also reviewed a management review of Milestone that HUD had conducted in 2002. However, we did not review or reach conclusions on Milestone's operations beyond the indicated timeframes.