Issue Date
February 20, 2009
Audit Report Number
2009-LA-1007

TO: William Vasquez, Director, Los Angeles Office of Community Planning and Development, 9DD

FROM: Joan S. Hobbs, Regional Inspector General for Audit, Los Angeles, 9DGA

SUBJECT: The City of Los Angeles Housing Department Did Not Always Ensure That Its HOME-Assisted Rehabilitation Work Was Complete and in Accordance with HOME Requirements

HIGHLIGHTS

What We Audited and Why

We audited the City of Los Angeles Housing Department (Department) as a result of an earlier audit of the HOME Investment Partnerships Program (HOME) affordability monitoring requirements and inspections of HOME-assisted rental units, which detected four projects that may not have been rehabilitated as intended. Our audit objective was to determine whether HOME funds were used as intended to rehabilitate the four projects and in accordance with HOME requirements.

What We Found

The Department did not always ensure that its HOME-assisted rehabilitation work was complete and in accordance with HOME requirements. Of the four projects, we found one project in which the Department paid $22,466 in HOME funds for incomplete rehabilitation work. In addition, it did not maintain agreements that described the use of HOME funds, such as the tasks to be performed. We attribute these deficiencies to the Department's inadequate policies, procedures, and controls to provide the required level of oversight to its HOME-assisted rehabilitation work projects.

What We Recommend

We recommend that the Director of the Los Angeles Office of Community Planning and Development require the Department to properly support or repay from nonfederal funds $22,466 in unsupported expenses. Additionally, we recommend that the Department develop, maintain, and implement operating policies and procedures regarding construction standards and construction monitoring for multifamily rehabilitation activities and establish quality control procedures for the construction monitoring functions.

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 report to the Department on February 3, 2009 and it provided its written response on Februrary18, 2009. The Department agreed with our finding 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. The Department's attachment to their response contained their draft revised policies and procedures, so we did not include them, but we will make them available upon request.

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BACKGROUND AND OBJECTIVE

The City of Los Angeles (City) is a participating jurisdiction overseen by the U.S. Department of Housing and Urban Development's (HUD) Office of Community Planning and Development, which executes the HOME Investment Partnerships Program (HOME). The City administers all of its HOME programs under the City of Los Angeles Housing Department (Department). Due to the variety of HOME program activities allowed under the law and the size of the entitlement grant, the Department divides its HOME program activities under the following major organizational units: the Major Projects Division manages the acquisition, new construction, or rehabilitation of large affordable rental housing projects; and the Homeownership and Preservation Division manages single-family or small multifamily purchase acquisition projects under its Homeownership Unit and manages single-family and small multifamily rehabilitation projects under its Preservation Unit.

The Department is the administrator of the City's HOME entitlement program. It follows monitoring standards and procedures to review and fund affordable housing developments to ensure compliance with HUD's program regulations. For example, it reviews the status of the HOME grant to ensure that the 24-month deadline to commit and five-year deadline to expend funds are complied with, monitors and reports on the HOME match requirements to ensure that the 12.5 percent match requirement is met, ensures that HOME-assisted rental units are inspected with the required frequency and comply with housing quality standards, and ensures that home-buyer and rental properties follow the applicable period of affordability. During the period of affordability, it reviews tenant household incomes and rents for compliance with HOME and other program requirements.

The objective of the audit was to determine whether HOME funds were used as intended to rehabilitate the four projects and in accordance with HOME requirements.

RESULTS OF AUDIT

Finding 1: The Department Did Not Always Ensure That Its HOME-Assisted Rehabilitation Work Was Complete and in Accordance with HOME Requirements

The Department did not always ensure that its HOME-assisted rehabilitation work was complete and in accordance with HOME requirements. Of the four projects reviewed, the Department paid $22,466 in HOME funds for incomplete rehabilitation work at one project. It also did not maintain agreements describing the use of HOME funds, such as the tasks to be performed. This condition occurred because the Department had inadequate policies, procedures, and controls to effectively monitor construction activities. As a result, neither the Department nor HUD was assured that the HOME funds were used for their intended purpose.

Rehabilitation Construction Deficiencies

Pursuant to 24 CFR [*Code of Federal Requirements*] 92.504(a), the Department had a responsibility to manage the day-to-day operations of its HOME program to guarantee that HOME funds were used in accordance with all program requirements. Three of the four projects reviewed had deficiencies. For one of the three projects, rehabilitation work was incomplete; however, payment had been disbursed to the developer. The other two projects had minor rehabilitation work deficiencies; for example, the rehabilitated work was completed, but the materials used were not those agreed upon. However, since the cost differences were not substantial, we did not recommend recovery of the related funds.

Examples of Deficiencies

For one of the four projects reviewed, the rehabilitation construction work required to be performed was not completed as specified, but the Department paid $22,466 in HOME funds to the developer. More specifically, carpet, medicine cabinets, and vanities with sinks were not installed in all of the units as described in the scope of work. Appendix D details the work items and related costs. The following pictures provide examples of the deficiencies observed.

None of the 30 units had carpets installed as indicated in the scope of work.

Only 1 of 17 bathrooms had bathroom cabinets installed as required. The remaining 16 bathrooms had only a shower and toilet as shown above.

Only 11 of 17 bathrooms had mirrors and medicine cabinets installed as required.

The problem occurred because the Department had inadequate policies, procedures, and controls to provide the required level of oversight to its HOME-assisted rehabilitation projects. These weaknesses resulted in the payment of $22,466 in HOME funding for unsupported rehabilitation expenses. Accordingly, HUD had no assurance that projects paid for with HOME funds were completed satisfactorily and in accordance with HOME requirements.

Agreements Not Maintained

Contrary to 24 CFR 92.504(b) (see appendix C), the Department did not maintain agreements before disbursing HOME funds to an entity. Of the four projects reviewed, two did not have the required written agreements. We were only able to locate preliminary work write-ups and spreadsheets. A construction specialist responsible for one of the two projects explained that projects originating in the Major Projects Division usually included plans but not final work write-ups or scopes of work (see appendix E). Consequently, we could not determine whether the projects paid for with HOME funds were completed as originally planned and agreed upon.

Conclusion

The problem occurred because the Department lacked current policies, procedures, and controls regarding the construction monitoring of its HOME projects, compounded by poor record keeping. We obtained a manual; however, the manual focused on the role of finance development officers rather than construction specialists, who are ultimately responsible for monitoring the construction of the projects. Without adequate procedures and controls, the Department may not have provided the required level of oversight to its HOME-assisted rehabilitation work projects to ensure that requirements were met. As a result, HUD may have provided HOME funding to projects that were not satisfactorily completed. Without adequate oversight, neither HUD nor the Department was assured that the HOME funds were used for their intended purpose. Department officials informed us that they were revising their policies and procedures to ensure the adequacy of the Department's oversight and record keeping.

Recommendations

We recommend that the Director of the Los Angeles Office of Community Planning and Development require the Department to

1A. Provide adequate support for the $22,466 in HOME funding for rehabilitation costs or repay this amount from nonfederal funds.

1B. Develop and maintain current operating policies and procedures regarding construction standards and construction monitoring for multifamily rehabilitation activities.

1C. Establish quality control procedures for the construction monitoring functions for projects managed in house.

SCOPE AND METHODOLOGY

We performed our on-site audit work at the Department, located in Los Angeles, California, between September and December 2008. Our audit generally covered the period of June 1999 through May 2006. We expanded our scope when necessary. Our objective was to determine whether HOME funds were used as intended to rehabilitate the four HOME projects and in accordance with HOME requirements.
To accomplish our audit objectives, we

- Interviewed HUD and the Department's personnel to acquire background information about the Department;
- Interviewed the Department's accounting department to obtain an understanding of its financial operations, practices, and controls;
- Reviewed the applicable federal laws, regulations, and HUD guidance for the HOME program;
- Reviewed the Office of Management and Budget (OMB) regulations for local grantees; and
- Reviewed the Department's accounting records, policies and procedures, and file documentation.

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 objectives are achieved:

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

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 objectives:

- Policies and procedures to ensure that HOME-assisted rehabilitation projects are carried out in accordance with applicable laws and regulations.
- Policies and procedures to ensure that HOME-assisted rehabilitation projects' expenditures are adequately supported.
- Policies and procedures to reasonably ensure that valid and reliable data are obtained and maintained.

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:

- The Department did not have adequate policies and procedures to ensure that rehabilitation construction for HOME projects was carried out in accordance with applicable laws and regulations (finding 1).

- The Department did not have adequate policies and procedures to ensure that HOME-assisted rehabilitation projects' expenditures were adequately supported (finding 1).

- The Department did not have adequate policies and procedures to reasonably ensure that valid and reliable data were obtained and maintained (finding 1).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Unsupported Costs 1/
1A	$22,466

1/ 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 the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures. The unsupported costs are HOME funds that the Department disbursed to the developer without adequate monitoring and record keeping for the rehabilitation construction of one of its HOME projects. It is the prorated amount expended on the project for which the Department was unable to provide adequate documentation to support the cost of rehabilitation.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Los Angeles Housing Department
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Antonio R. Villaraigosa, Mayor
Mercedes Márquez, General Manager

February 18, 2009

Tanya Schulze
Office of the Inspector General
U.S. Department of Housing and Urban Development
Los Angeles Field Office, Region IX
611 W. 6th Street, Suite 1000
Los Angeles CA 90017

RE: HUD Management Decision on Draft Audit Report No. 2009-LA-100x.
Los Angeles Housing Department Rehabilitation of Four HOME-funded Projects

Dear Ms. Schultz,

Attached please find the Los Angeles Housing Department's response to the Draft Audit Report.

FINDING 1 – LAHD did not always ensure completion of work in accordance with HOME requirements

Recommendation 1A – Provide adequate support for the $22,466 in HOME funding for rehabilitation costs or repay this amount from nonfederal funds.

Comment 1

LAHD Response: The Department will repay $22,466 from nonfederal funds. This project applied for funds in February 1999 and was completed in 2005. As noted in the audit report, we cannot confirm that all of the items under the original work order, such as medicine cabinets, were in fact installed, because the files lack complete documentation. The staff that worked on this project are no longer with the LAHD, and without their input, it is not possible to recreate what took place with this project. However, we note that the funds in question were in fact used for eligible HOME expenses (permits).

Recommendation 1B – Develop and maintain current operating policies and procedures regarding construction standards and construction monitoring for multifamily rehabilitation activities.

LAHD Response: The Department recently finalized written policies and procedures for its Major Projects Division, including specific guidance for the Construction Services Unit. Although pending final adoption in the next month, the construction standards and monitoring procedures have been in use since 2006 (please see Attachment 1 – Major Projects Policies & Procedures). The policies and procedures discuss how the construction standards are established in a project's Construction Contract Documents;

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specifically the Specifications (see Sections 3.1 and 4.2); as well as the requirements for construction monitoring.

Recommendation 1C – Establish quality control procedures for the construction monitoring functions for projects managed in house.

As described in the operating policies and procedures, during the development of the plans and specifications, our Architect reviews these items at three stages: conceptual, schematic, and post plan check, for compliance with our Architectural Guidelines. The Rehabilitation Construction Specialists review the approved specifications and make sure that they are followed as part of the construction monitoring process as the job progresses. The Rehabilitation Construction Specialists monitor the project for quality control, at minimum, on a monthly basis consistent with the draw requests and payments (see Section 3.5). In addition, our Policies and Procedures require additional monitoring by the Rehabilitation / Construction Specialists' supervisors at the 30%, 60% and 100% completion intervals for further verification.

In closing, this audit was helpful in highlighting problems of the past. LAHD is committed to moving into the future with an efficient, effective program that is in compliance with HUD regulations. If you have any questions about the materials provided or items that you feel have not been fully addressed in this submission, please contact Marlene Garza, Assistant General Manager, either by phone (213) 808-8899 or by email mgarza@lahd.lacity.org.

Sincerely,

MERCEDES MÁRQUEZ
General Manager

Attachment – Major Projects Policies & Procedures

OIG Evaluation of Auditee Comments

Comment 1 We would like to note that the questioned costs were not for permits, as stated. Rather, the funds in question were for carpet, medicine cabinets, and vanities with sinks as described in the scope of work.

Appendix C

CRITERIA

A. 24 CFR Part 92, Home Investment Partnerships Program

- **24 CFR 92.504(a)** states, "The participating jurisdiction is responsible for managing the day to day operations of its HOME program, ensuring that HOME funds are used in accordance with all program requirements and written agreements, and taking appropriate action when performance problems arise. The use of State recipients, subrecipients, or contractors does not relieve the participating jurisdiction of this responsibility. The performance of each contractor and subrecipient must be reviewed at least annually."
- **24 CFR 92.504(b)** states, "Before disbursing any HOME funds to any entity, the participating jurisdiction must enter into a written agreement with that entity, a State recipient, subrecipient, or contractor which is administering all or a part of the HOME program on behalf of the participating jurisdiction, must also enter into a written agreement with that entity……"
- **24 CFR 92.504(c)** states, "The contents of the agreement may vary depending upon the role the entity is asked to assume or the type of project undertaken. This section details basic requirements by role and the minimum provisions that must be included in a written agreement."
- **24 CFR 92.504(c)(1)(i)** states, "The agreement must describe the use of the HOME funds, including the tasks to be performed, a schedule for completing the tasks, and a budget. These items must be in sufficient detail to provide a sound basis for the State to effectively monitor performance under the agreement."
- **24 CFR 92.508(a)** states, "Each participating jurisdiction must establish and maintain sufficient records to enable HUD to determine whether the participating jurisdiction has met the requirements……"
- **24 CFR 92.508(a)(3)(ii)** requires records demonstrating the source and application of funds of each project, including supporting documentation in accordance with 24 CFR 85.20.
- **24 CFR 92.508(a)(6)** requires records demonstrating compliance with the written agreements required by Section 92.504.
- **24 CFR 92.251(a)(1)** states, "Housing that is constructed or rehabilitated with HOME funds must meet all applicable local codes, rehabilitation standards, ordinances, and zoning ordinances at the time of project completion……"

B. Cost Principles for State, Local, and Indian Tribal Governments (OMB Circular A-87)

- **2 CFR Part 225** requires costs claimed under federal awards to be reasonable and adequately documented. In determining the reasonableness of a given cost, consideration shall be given to market prices for comparable goods and services.

C. Administrative Requirements for Grants and Cooperative Agreements to State, Local, and Federally Recognized Indian Tribal Governments

- **2 CFR Part 85. 20** states, "A state must expand and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds…"

D. OMB Circular A-133, subpart C(.300b), states, " the auditee shall: (b) maintain internal control over federal programs that provides reasonable assurance that the auditee is managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements that could have a material effect on each of its federal programs……"

Appendix D

SCHEDULE OF UNSUPPORTED COSTS

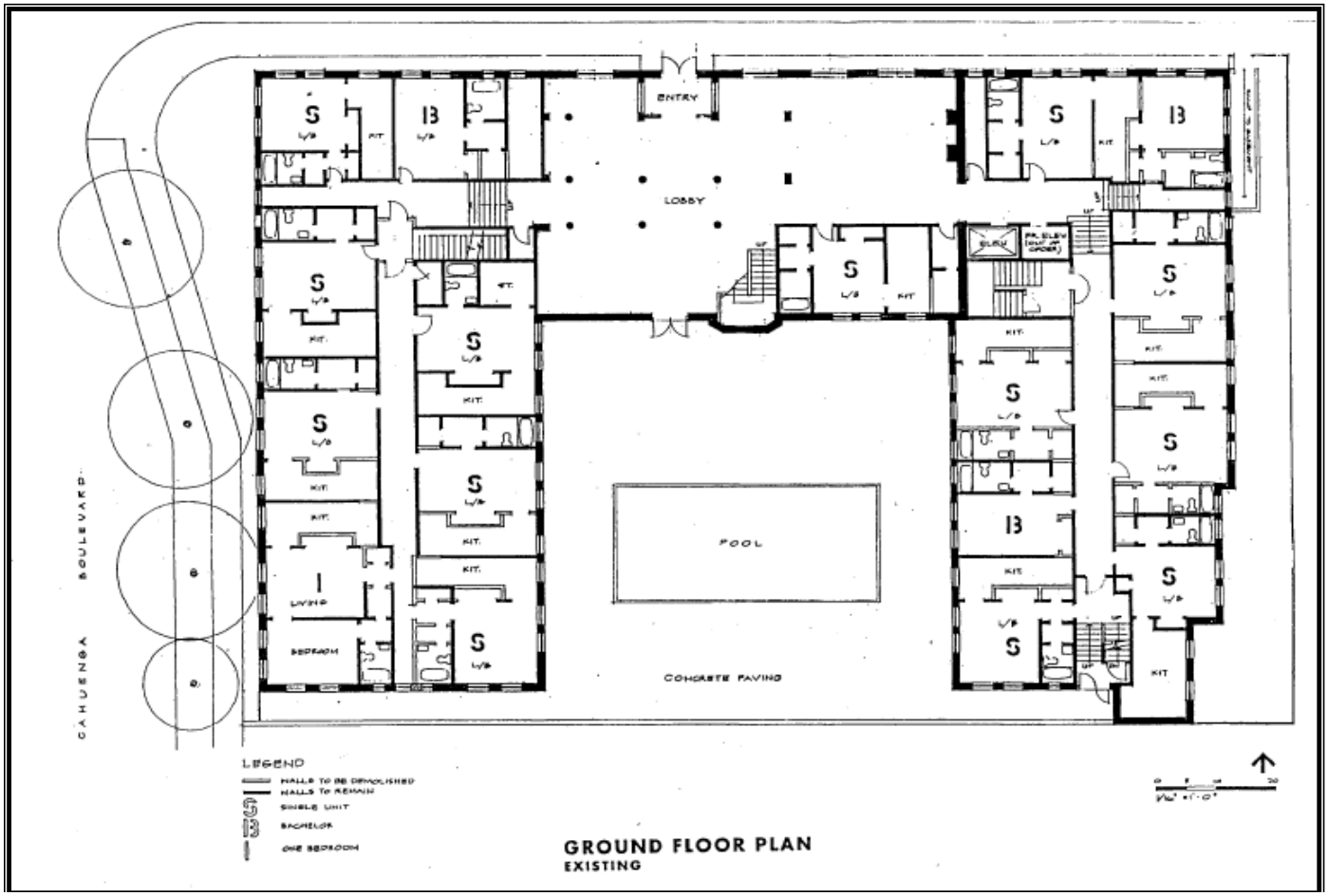
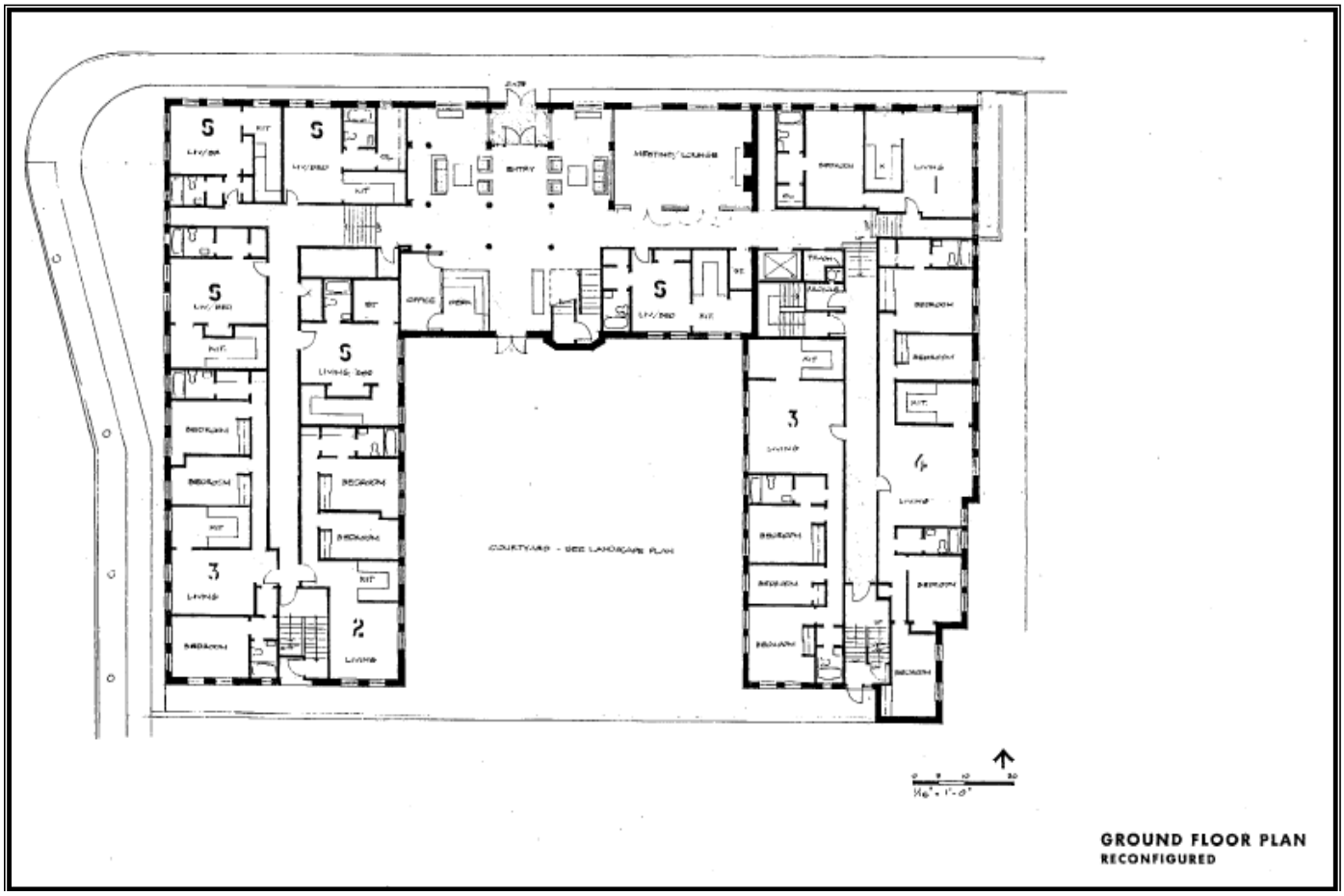
	A	B	C	D	E	F	G	
Rehabilitation work item	**Work item contract amount**	**Number of units with uncompleted rehabilitation work**	**Number of units in which required work was completed**	**Cost per unit for uncompleted rehabilitation work (A/17 bathrooms)**	**Cost per unit for uncompleted rehabilitation work (A/30 units)**	**Unsupported cost (DxB)**	**Unsupported cost (ExB)**	**Total unsupported costs**
Bath cabinets	$6,000	16	1	$353	NA	$5,648	NA	$5,648
Installation of bath cabinets	$4,000	16	1	$235	NA	$3,760	NA	$3,760
Vanity with sink	$1,200	14	3	$71	NA	$994	NA	$994
Mirrors and medicine cabinets	$1,600	6	11	$100	NA	$564	NA	$564
Carpet	$8,500	30	0	NA	$283*	n/a	$8,500*	$8,500
Installation of carpet	$3,000	30	0	NA	$100	n/a	$3,000	$3,000
							Total:	**$22,466**

*The exact cost per unit is $283.33. The total unsupported cost is $8,500 ($283.33 x 30 units).

Appendix E

EXAMPLE OF PLANS USED INSTEAD OF SCOPES OF WORK

Existing plan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