U. S. Department of Housing and Urban Development
Office of Inspector General
26 Federal Plaza, Room 3430
New York, NY 10278 0068

MEMORANDUM NO: 2010-NY-1803

March 12, 2010

MEMORANDUM FOR: Mirza Negron Morales, Director, Office of Public Housing, 2APH

FROM: Edgar Moore, Regional Inspector General for Audit, New York/New Jersey, 2AGA

SUBJECT: The New York City Housing Authority Had the Capacity to Administer Capital Funds Provided Under the American Recovery and Reinvestment Act

INTRODUCTION

We performed a review of the New York City Housing Authority's (Authority) capacity to administer the approximately $423 million in capital funds awarded under the American Recovery and Reinvestment Act of 2009 (Recovery Act) in support of the Office of Inspector General's (OIG) goal to report on Recovery Act recipients' capacity to administer funds received. The Authority was selected based upon an OIG risk assessment of Recovery Act recipients in which the Authority ranked high because of (1) its 2009 U.S. Department of Housing and Urban Development (HUD) designation as a high-risk public housing authority and (2) weaknesses in the administration of its Public Housing Capital Fund (Capital Fund) program previously reported by OIG,[1] its inspector general,[2] and a consulting firm.[3] The objective of the review was to determine whether the Authority's general, financial, and procurement controls were adequate to provide assurance that it had the capacity to effectively manage the Recovery Act funds.

We discussed the contents of this memorandum with Authority officials during the review and provided them a draft memorandum on February 22, 2010, which was discussed at an exit conference on March 1, 2010. We received written comments on March 5, 2010, which are included in Appendix A. Authority officials generally agreed with our findings and have initiated action to respond to the recommendations.

[1] The New York City Housing Authority, New York, New York, Had Administrative Weaknesses in its Capital Fund Program (report number 2009-NY-1002), issued November 25, 2008.
[2] Inspector General Office (IGO) Investigation of NYCHA's CM/Build Program, issued September 17, 2008.
[3] The consultant issued the following: New York City Housing Authority Capital Program and Project Management Processes Assessment, issued December 18, 2008, and a 2009 Follow-Up Assessment, issued July 31, 2009.

This report contains five recommendations. 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 review.

METHODOLOGY AND SCOPE

Our review was primarily limited to gaining an understanding of the Authority's internal controls over and plans for the administration of the capital funds received under the Recovery Act. To accomplish our objectives, we (1) reviewed laws, regulations, and HUD guidance applicable to both the Recovery Act and the Capital Fund program, and (2) documented corrective action taken in the administration of the Capital Fund program in response to a HUD field office monitoring report and prior reports issued by the Authority's inspector general, a consultant, and HUD OIG. In addition, we interviewed HUD field office officials and the Authority's procurement, finance, and capital projects staff. To gain a better understanding of the internal controls over Recovery Act funds, we reviewed the Authority's policies and procedures, annual and five year plans, board resolutions, procurement files, and financial reports. To test the internal controls, we reconciled Recovery Act-funded projects to internal financial reports and HUD's Line of Credit Control System and selected a nonstatistical representative sample of 10 contracts executed between April and August 2009 to assess whether the procurements complied with Recovery Act and Authority requirements. We tested approximately $42.5 million, representing 29 percent of the $146.8 million that was obligated as of August 31, 2009. We performed our on-site work from August 2009 through January 2010 at the Authority's offices located in New York City, NY. The review period was January 1, 2008, through August 31, 2009, and was expanded as deemed necessary.

For this capacity review, our work was not conducted in accordance with generally accepted government auditing standards. Under the Recovery Act, inspectors general are expected to be proactive and focus on prevention; thus, this report is significantly reduced in scope.

BACKGROUND

The Recovery Act, enacted on February 17, 2009, included a $4 billion capital fund appropriation for public housing agencies to carry out capital and management activities as authorized under Section 9 of the United States Housing Act of 1937. The Recovery Act requires that $3 billion of these funds be distributed as formula grant funds and the remaining $1 billion be distributed through a competitive process.

The Recovery Act provides stricter obligation and disbursement deadlines than the standard Capital Fund program. Recipients must obligate 100 percent of the funds within 1 year of the date the funds become available for obligation, expend at least 60 percent within 2 years, and expend 100 percent of the funds within 3 years. The Recovery Act provides for recapture and reallocation of any funds that do not comply with these deadlines.

On March 18, 2009, the Authority received approximately $423 million in Recovery Act capital funds. This amount represents a 27 percent increase over its fiscal year 2008 Capital Fund program

grant of $334.4 million. The Authority plans to use the Recovery Act funds for capital projects, including elevator repairs; boiler replacements; and other maintenance, repair, and energy efficiency projects in its developments.

RESULTS OF REVIEW

Our limited review indicated that the Authority's general, financial, and procurement controls were generally adequate to provide assurance that it had the capacity to effectively manage its Recovery Act funds. Authority officials had plans for using the funds in a timely manner and had addressed previously reported weaknesses in its Capital Fund program administration. Nevertheless, HUD needs to closely monitor the Authority to ensure that it will achieve planned accomplishments within the prescribed timeframes and take action necessary to ensure compliance with Recovery Act requirements.

Authority Plans to Obligate Funds Within Prescribed Timeframes

If Authority officials' plans for the Recovery Act funds are implemented, the funds will be obligated by the March 17, 2010, deadline and used for eligible activities that meet the objectives of both the Capital Fund program and the Recovery Act. As of December 31, 2009, Authority officials had obligated $346.4 million, or 81 percent, of the $423 million awarded. Authority officials were pursuing two alternatives for the obligation of the remaining funds. The alternative chosen will depend upon HUD's approval of a mixed-finance proposal. Under the first alternative, Authority officials plan to use approximately $116 million in Recovery Act funds to support a mixed-finance modernization plan to federalize 21 State- and city-built developments. Funding for the modernization plan would be supplemented with Federal low-income housing tax credits and tax-exempt bonds, which Authority officials plan to market in March 2010. Authority officials responded to comments raised on January 6 and 8, 2010 by HUD headquarters about this plan after HUD's initial review of the proposals,[4] and received HUD approval of the plan on February 26, 2010. After the Authority completes closing on the properties and executes an annual contributions contract with HUD, the plan can proceed. Once the modernization plan is finalized, the Authority plans to deobligate Recovery Act funds that have already been earmarked for specific Recovery Act-eligible projects to help meet the $116 million proposed mixed-finance modernization plan cost. The alternative would be to obligate the remaining funds for other Recovery Act-eligible contracts within the prescribed timeframe.

Approximately $234.5 million, or 68 percent, of the Recovery Act funds obligated as of December 31, 2009, were awarded under the construction management (CM)/Build[5] concept. Since CM/Build firms do not perform the construction work, accomplishment of work and the expenditure of funds are dependent upon the award and performance of subcontracts. Consequently, Authority officials need to actively monitor these firms' progress to ensure that subcontracts are awarded in a timely manner and that obligated funds will be expended as planned by the established deadline. As of December 31, 2009, $91.3 million, or 39 percent, of the $234.5 million had been awarded to subcontractors. While

[4] The modernization plan contains two proposals: a tax credit portion and non-tax credit portion.
[5] Under the CM/Build concept, the Authority contracts with a firm to perform construction management services for a fee, and the firm subcontracts for and monitors the actual construction work.

the funds are considered obligated at the time the CM/Build contract is awarded, actual subcontracts may be awarded after a significant passage of time. For example, in six instances, approved subcontracts were awarded between 4 and 7 months after the CM/Build task orders were issued.

Actions Had Been Taken To Strengthen Controls

Authority officials had taken actions to address weaknesses previously reported in the administration of the Capital Fund program. In November 2008, a HUD OIG report noted that the Authority lacked adequate controls to track the obligation and deobligation of capital funds associated with specific contracts when fungibility[6] was applied. In response, Authority officials generated a monthly report from their financial reporting system that supports amounts obligated under the Capital Fund program with specific contract information. For the period reviewed, these reports reconciled to the amount reported as obligated in HUD's Line of Credit Control System; however, we could not test whether the report properly accounts for fungibility since the Authority did not employ fungibility with Recovery Act funds during the period of our review. Moreover, HUD officials stated that they had not completed an evaluation of the report to conclude that it will effectively track expenditures associated with contract deobligation and reobligation activities as recommended in the previous OIG report.

In September 2008, the Authority's inspector general reported a number of weaknesses, particularly poor cost estimating procedures relating to CM/Build contracts, which resulted in the completion of 39 of 100 scheduled projects financed with $300 million in bond proceeds. In response, Authority officials reorganized the Authority's Capital Projects Division and implemented procedures to strengthen controls to address the reported weaknesses. While the inspector general report noted that cost estimates were much lower than actual contract awards, in the 10 contracts we reviewed, the cost estimates were on average 4 percent greater than the actual contract awards.

In December 2008, a consultant recommended that the Authority develop a consolidated Capital Projects Division policies and procedures manual. Therefore, Authority officials were developing a consolidated policies and procedures manual as recommended. Further, in response to a recommendation by the independent public accountant after the audit for the year ending December 31, 2008, the Authority began to formulate a standard procedure for documenting the roles and responsibilities of the different departments responsible for the administration of capital funds. This procedure was circulated for comment in October 2009, but a timetable for completion had not been established.

Actions Are Needed to Ensure Compliance with the Authority's Procurement Policy

The Authority's Contract Procedure Resolution – Stimulus Procurement Policy provides that all Authority contracts must contain appropriate provisions. However, 7 of 10 contracts reviewed did not

[6]Regulations at 24 CFR (Code of Federal Regulations) 968.305 allow Capital Fund program grant recipients to exercise fungibility when obligating funds. Fungibility is defined as a concept which permits the substitution of any work item from the latest approved five year action plan to any previously approved budget and to move work items among approved budgets without prior HUD approval.

contain provisions related to energy efficiency[7] and "Buy American."[8] Authority officials did not address the energy efficiency provisions, but stated that HUD guidance on the implementation of the "Buy American" provision was not received until May 2009. After HUD guidance was received, Authority officials promulgated an e-mail on May 13, 2009 containing a proposed "Buy American" provision, which was to be added to the General Conditions section of contracts awarded after that date. However, three of six contracts awarded after May 13, 2009, did not contain the provision. This omission occurred because the contracts' General Conditions section was provided as part of the bid package before that date. In addition, Authority officials had not developed written procedures to verify and document the contractors' compliance with the "Buy American" requirement.

The Authority's Contract Procedure Resolution - Stimulus Procurement Policy requires that records be maintained that detail a contract's procurement history. However, Authority records for 4 of 10 procurements we reviewed did not document the resolution of vendor name checks conducted during the procurement process that disclosed potentially derogatory contractor information. While a July 9, 2009, review recommended follow-up to assess a company's financial capacity to perform proposed work, Authority officials awarded a contract on July15, 2009, for the work without documentation in the file showing that the issue had been resolved. In a second case, the contract file contained no verification of a proposed contractor's claim that a questioned loan had been repaid, and in the last two cases,[9] the files did not address whether a contractor's loan arrangement posed financial concerns for the Authority. An Authority official stated that although documented follow-up action was lacking, the issues had been resolved because without such resolution, the contracts would not have been awarded.

RECOMMENDATIONS

We recommend that the Director of the New York Office of Public Housing

1A. Closely monitor, through on-site visits or remotely, the status of contracts used to obligate Recovery Act funds, which may be substituted with modernization proposal obligations if approved in time to obligate Recovery Act funds, and reconcile the Authority's monthly contract report if fungibility is employed on Recovery Act-funded contracts to ensure compliance with applicable obligation and expenditure requirements.

1B. Review the CM/Build firms' progress in awarding subcontracts to ensure that they are awarded in a timely manner, thus providing greater assurance that funds will be expended by the March 17, 2012, deadline.

1C. Instruct the Authority to strengthen controls over the administration of Recovery Act and Capital Fund program funds by (1) finalizing the consolidated policies and procedure manual and the

7 Mandatory standards and policies for energy efficiency are contained in a New York State energy conservation plan, issued in compliance with the Energy Policy and Conservation Act (Public Law 94-163).

8 Section 1605 of the Recovery Act requires that none of the funds appropriated or otherwise made available by the Recovery Act may be used for a project for the construction, alteration, maintenance, or repair of a public building or public work unless all of the iron, steel, and manufactured goods used in the project are produced in the United States.

9 The third and the fourth cases pertain to the same contractor awarded two separate contracts.

procedures to document the roles and responsibilities of different departments responsible for the administration of capital funds and (2) ensuring that resolution of any potentially derogatory contractor information revealed during the procurement process is documented.

1D. Direct the Authority to update the General Conditions section of the contract to ensure that it contains the appropriate provisions related to energy efficiency and "Buy American" as mandated by the procurement policy.

1E. Instruct the Authority to develop written procedures to verify and document contractors' compliance with the "Buy American" requirement of the Recovery Act.

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

NEW YORK CITY HOUSING AUTHORITY

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Mr. Edgar Moore
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
26 Federal Plaza
New York, New York 10278
March 5, 2010

Dear Mr. Moore:

The New York City Housing Authority is providing the following comments to your draft memorandum # 2010-NY-180X addressed to Ms. Negron Morales, Director, Office Public Housing which was forwarded to Michael Kelly, General Manager of the New York City Housing Authority.

The Capacity review states that " Approximately $234.5million or 68 percent, of the Recovery Act funds obligated as of December 31, 2009, were awarded under the construction management (CM) Build concept."

NYCHA's Response

Comment 1

As of February 28, 2010; NYCHA has obligated $403,050,967.04 or 95% of the Recovery Act funds. $226.5M has been awarded in 15 Task Orders to CM firms, representing 56% of the total obligated. Of the $226.5M awarded to CM firms, $115M has been awarded in 21 subcontracts to date. representing 51% of the total awarded to CM firms, or 29% of the total $403 million obligated.

HUD OIG Recommendation 1B
The HUD Office of the Inspector General indicated that the Director of New York Office of Public Housing "Review the CM/Build firms' progress in awarding subsontracts to ensure that they are awarded in a timely manner, thus providing greater assurance that funds will be expended by March 17, 2012, deadline"
NYCHA's Response to 1B
Under the original stimulus plan, 15 of the stimulus projects were assigned to CM/Build firms. As of February 28, 2010, construction subcontracts for 11 of these projects have been awarded. Two (2) of the non-awarded contracts comprising the Whitman Ingersoll

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Comment 2

project will be transferred to the federal capital program in order to fund the 27 contracts in the federalization plan. The final two (2) projects were bid and are in the award process. All of the 27 federalization projects that will be added to the stimulus program have already been bid and awards are pending the closing of the federalization deal.

HUD OIG Recommendation 1 C

"Instruct the Authority to strengthen controls over the administration of Recovery Act and Capital Fund program funds by (1) finalizing the consolidated policies and procedures manual and the procedures to document the roles and responsibilities of different departments responsible for the administration of capital funds and (2) ensuring that resolution of any potentially derogatory contractor information revealed during the procurement process is documented."

NYCHA's Response to 1C

Comment 3

1) The consolidated procedure manual was drafted on February 2, 2010 and will be finalized by March 19th.
2) The procedures to document the roles and responsibilities of different departments responsible for the administration of capital funds will be finalized before March 31, 2010 and will be referenced in the consolidated Capital Projects Department policies and procedures manual.

HUD OIG Recommendation 1 D

"Direct the Authority to upgrade the General Conditions section of the contract to ensure that it contains the appropriate provisions related to energy efficiency and "Buy American" as mandated by the procurement policy"

NYCHA's Response to 1D

Comment 4

The General Conditions were updated to include the "Buy American" provisions and amendments were issued for the contracts that were bid without it. NYCHA's development of a "Buy American" provision for its contracts prior to May 13, 2009, was hindered by the absence of specific guidance from HUD clarifying how the "Buy American" requirement should be implemented. PIH 2009-12 (HA), which was issued by HUD on March 18, 2009, and only stated that "PHAs shall follow Buy American requirements of section 1605 of the Recovery Act and use only iron, steel and manufactured goods produced in the United States in their projects," was not formally expanded upon by HUD with specifics as to implementation of the "Buy American" requirement until PIH 2009- 31 (HA) was issued on August 21, 2009. Nonetheless, NYCHA endeavored to implement the Buy American requirement beginning in May 2009.

NYCHA will incorporate the energy efficiency requirement and amend the contracts accordingly.

HUD OIG Recommendation 1 E

"Instruct the Authority to develop written procedures to verify and document contractors' compliance with the "Buy American" requirement of the Recovery Act"

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Comment 5

NYCHA's Response to 1E
Procedures for verifying and documenting compliance with the "Buy American" requirement are included in the policy and procedure manual.

We appreciated working with you and your team

Michael Kelly
General Manager

OIG Evaluation of Auditee Comments

Comment 1 Amounts we reported awarded under the CM/Build concept and to subcontractors as of December 31, 2009 are based upon data provided by the auditee prior to the exit conference. Subsequent to the exit conference the auditee reported updated data as of February 28, 2010. The updated data indicates that the amount awarded CM/Build contractors decreased from 68 percent to 56 percent of the total amount obligated. Further, the amount awarded subcontractors increased from 33 percent to 51 percent of the amount awarded CM/Build firms. While we have not had the opportunity to verify the updated data, the recommendation is still pertinent. Given the significant amount awarded CM/Build contractors, continued review of CM/Build firms' progress in awarding subcontracts is warranted to ensure that they are awarded in a timely manner, thus providing greater assurance that funds will be expended by the March 17, 2012, deadline.

Comment 2 The auditee reports that of the 15 planned projects to be awarded CM/Build firms, two will be transferred to the federalization plan and the final two projects were bid and are in the award process. Consequently, continued review of CM/Build firms' progress in awarding subcontracts is warranted to ensure that they are awarded in a timely manner, thus providing greater assurance that funds will be expended by the March 17, 2012, deadline.

Comment 3 Actions planned, and being taken, by the auditee are responsive to recommendation 1C. The evidence necessary to close this recommendation will be the finalized Capital Projects Department policies and procedures manual documenting departments' roles and responsibilities, including ensuring resolution of any derogatory contractor information revealed during the procurement process.

Comment 4 Based on the auditee's comments we changed the report to reflect that Authority officials did not receive guidance about "Buy American" until May 2009. Nevertheless, the auditee's ongoing and planned actions are responsive to the recommendation. Therefore, the evidence necessary to close this recommendation will be the amended contracts and updated "General Conditions" section of contracts.

Comment 5 Actions being taken by the auditee are responsive to the recommendation. Therefore, evidence necessary to close this recommendation will be the finalized Capital Projects Department policies and procedures manual.