U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410-4500

OFFICE OF THE INSPECTOR GENERAL

November 4, 1988

Exhibit 17

MEMORANDUM FOR: J. Michael Dorsey, General Counsel, G

FROM: Paul A. Adams, Inspector General, Z

SUBJECT: Section 8 Moderate Rehabilitation Funding Decisions

This is a follow-up to my memorandum dated October 28, 1988 regarding the FY 1989 Section 8 Moderate Rehabilitation Funding. I have continuing concerns and am bringing to your attention some information developed during our ongoing reviews. My staff has reviewed the FY 1989 process to date and found that little was done to address the concerns we expressed to Tom Demery and you at our meeting on September 16, 1988. Also, Larry Goldberger's memorandum dated October 18, 1988 to Tom Demery stating that OIG concerns were resolved is incorrect.

FY 1988 FUNDING PROCESS

We reviewed the process followed for the July 1988 moderate rehabilitation funding round and found several inconsistencies in the manner in which applications were rated and ranked. Consequently, we believe several PHAs were inappropriately selected for funding in July 1988. In addition, Mr. Demery allocated certain PHAs more units than recommended and allowed certain PHAs additional consideration that enabled them to obtain higher scores for the financing factor. The following summarizes the conditions we noted:

Unit allocation raised by the Assistant Secretary

The Committee advised the Assistant Secretary as to what PHAs should be funded and suggested the distribution of units. Three PHAs had their unit allocations raised by the Assistant Secretary. We found no information that would support an increase in the number of units. The changes were as follows:

PHA	Units Applied For	Suggested Units	Units Awarded
H.A. of Midland Co., TX	175	100	125
H.A. of Salt Lake City*	150	100	125
H.A. of the City of Temple, TX*	100	25	50

*As discussed later, these PHAs also received additional consideration to bring them up to a fundable level.

In the Midland application the Committee suggested 100 units be funded. The Committee commented, "100,000 population with very few vouchers/certificates." In essence, the Committee felt that 100 units was a generous allocation as other applicants received about one third of the units they requested. The evaluator commented on the Midland application, "PHA, if selected, must be reminded of need to conduct public notice/competitive selection based on HUD approved Administrative Plan. Application indicates that they are definitely considering a particular project, but do not state it was selected competitively." The Assistant Secretary changed the number of units to 125. Our auditors determined that the Midland County PHA advertised prior to receiving the allocation. The PHAs most preferred project is a 125 unit building controlled by George Carnes and David Barrett. Mr. Barrett was in frequent communication with Mr. Demery during the period that selections were made.

The Committee recommended 100 units of the Salt Lake City application be funded. The Committee commented that 100 units would be "consistent with previous [decisions]." The Assistant Secretary changed the number of units to 125. The initial application gave no information as to a specific project. This was one of the applications where additional financing information was provided (discussed later). The supplemental financing information identified two specific projects accounting for 128 of the 150 units applied for. The developers controlling the 128 unit projects are Pingree and Dahle, a firm with substantial MRP experience. Martin Artiano, who was in frequent communication with Mr. Demery, is also a principal in the project.

The Committee recommended 25 units of the Temple, Texas application be funded. The Committee commented that only 25 units should be funded because it is a new program. The Assistant Secretary changed the number of units to 50. The application does not identify any specific projects. However, the application states that "one potential owner has outside financing readily available."

Some PHA's were given additional consideration for the financing factor

The Committee rated all applications and provided a ranked list of fundable applications to the Assistant Secretary. The Assistant Secretary noted that twelve applications scoring 44 points or more received weak ratings for the financing factor. The Assistant Secretary decided to re-examine these applications and, if necessary, contact the PHAs to determine if they had additional financing information as of the application date. Some financing scores were changed based on a re-examination of the original application, while other PHAs submitted additional information which raised their scores. The following is a list of the PHAs and their revised scores:

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PHA	Committee Initial Score	New Committee Score After Reconsideration of financing
Temple, TX*	47	48
Los Angeles*	47	48
Boise, ID	47	48
Howard Co., MD	46	48
Salt Lake City*	46	48
Linn-Benton	46	No change
Montana*	44	48
West Va. H.A.	48	49
Arlington, VA	48	No change
Miami*	48	49
Portage, OH*	48	No change
Idaho HFA	48	No change

*funded 7/88

While it appears that all applicants were given the same consideration, several other applications, falling below 44 points, could have scored high enough to be funded. These applicants were not given an opportunity to provide additional financing information to raise their scores. These applicants did not reach the 44 points because their rating for overall feasibility was low. The rating for overall feasability is an evaluation of the 4 other factors. Over one half of the applications funded in July 88 did not receive maximum scores in the four other factors yet received a maximum score for overall feasibility. With additional financing information the overall feasibility and financing score would be raised to a fundable level. The following is a list of those PHAs that did not get the opportunity to provide additional financing information.

PHA	Rehab Exp	Fin.	Admin Cap	Rehab/ Leasing	Overall Feas.	Comm. Score	Potential 1 Score
Manchester N.H.*	15	3	10	3	12	43	48
Franklin Co. MA*	15	4	10	3	12	44	48
Erie County NY	15	0	10	3	9	37	48
Virginia HDA*	15	3	10	3	9	40	48
KY Hsg. Corp.*	15	2	10	5	9	41	50
Bowling Green KY	15	2	10	0	12	39	45
Ft. Worth HA	15	0	10	2	9	36	47
North Dakota HA*	15	2	10	5	12	44	50
Vancouver WA HA*	15	1	10	3	12	41	48
Maximum Scores	15	5	10	5	15	50	

1 The potential score is based on the PHA providing all necessary financing information and receiving a score of 5 points which in turn would raise the overall feasibility score to 15 points.

* These six projects could have received high enough scores to be funded in July 1988. They received no funding in FY 1989 either.

Rehabilitation and leasing schedules not consistently ranked

One of the more objective ranking factors is the PHA's ability to achieve a timely rehabilitation and leasing of the units. In the application, the PHA is asked to provide a 24-month schedule showing when all units applied for will be under agreement and leased. Since most PHAs applied for considerably more units than could be funded, most identified a full 2 year schedule in completing all the units. PHAs identifying a full 2 years to process the units were rated adequate for this factor. PHAs showing a rehabilitation and leasing schedule within 18 months were given an excellent rating in this ranking factor. Except for two applications, the evaluators did not give weight to the fact that; (1) fewer units can be completed in a shorter time frame, and (2) most applicants would be funded for fewer units. The 31 PHAs selected for funding received an average of 35 percent of the units they applied for. In two of the funded applications, the rehabilitation and leasing rating factor was raised based on the evaluator's decision that a lesser number of units would be approved.

The application for the Housing Authority of the City of Temple, Texas identified a 21-month rehabilitation and leasing schedule for the 100 units in their application. Initially, the PHA received an adequate rating for the rehabilitation and leasing factor. The committee raised this rating factor to excellent in consideration of funding one half of the units applied for. This application would not have been funded unless this rating factor was raised. (This action changed the total rating to 47 from 46. As discussed previously, Temple's score was later raised for the financing factor.)

In the New Orleans CIA application, the PHA indicated that the 419 units applied for would be completed in 12 months. Two initial raters of the application felt this was an unrealistic schedule. Based on prior PHA experience, this factor was rated adequate. This rating was later raised to excellent by the Office Director in consideration of funding for a reduced number of units. Without the higher rating, this application would not have been funded.

Several other PHA applications were not funded because they received an adequate rating for the rehabilitation and leasing schedule ranking factor. We identified six applications receiving perfect scores in all ranking factors except for this factor. If consideration was given to funding a lesser number of units, their rankings would have been raised. As seen in the chart below, consideration to funding 50 percent of the units applied for would have brought four of the PHAs' ratings to excellent (within 18 months).

PHA	Number of Units in Application	Scheduled # of Months to Complete	Scheduled # of Months to Complete 50% of Units
Macon, Georgia	120	21	15
Cuyahoga MHA	400	24	21
St. Paul H.A.	100	24	15
Santa Cruz, CA	200	24	18
Everett H.A.	85	24	21
Portland H.A.	100	24	15

Management Information System data applied inconsistantly

The PHA's record in managing previously funded moderate rehabilitation units is a major consideration in the rating process. Past experiences are important in determining the PHA's rehabilitation expertise and their ability to achieve a rapid rehabilitation and leasing schedule for any newly awarded units. A record of previously funded moderate rehabilitation projects is taken from the Management Information System (MIS) and included on the Application Review Checklist. We found that the MIS was not reliable in identifying the PHA's past record. During this evaluation process, the MIS information was inconsistently used.

The MIS identified nine previously funded Michigan State Housing Development Authority (HDA) moderate rehabilitation projects with no units completed. Since none of the previously funded projects were complete, the rater noted on the review sheet, "Assume PHA has completed projects on schedule and MIS data is severely deficient." This PHA was then rated excellent for the factor on Rehabilitation Expertise and the factor on Rehabilitation and Leasing Schedule. Michigan State HDA was awarded 150 units in the July 1988 funding round. In looking behind the MIS information, we found two incomplete Michigan State HDA moderate rehabilitation projects, one of which was funded in 1984. If this information was known during the rating process, the PHA should not have received an excellent rating. Evidence that the PHA could not complete the units within the estimated time frame should have resulted in a lower evaluation score. With a lower score, Michigan State HDA would not have been funded.

In contrast, the Oklahoma HFA application was not funded because of reliance on the MIS. The MIS identified four incomplete projects for this PHA, funded in 1985 and 1986. Because the evaluator relied on the MIS, the application was rated adequate for rehabilitation expertise. This rating resulted in a lower total score and the application not being referred to the committee for consideration. In checking with the PHA, we found the MIS information was incorrect and all four projects were completed. If the correct information had been known, it is likely that the application would have received a high enough rating to be funded.

In the Richmond PHA application, Richmond pointed out that 282 previously funded moderate rehabilitation units were in process. The MIS confirmed that some of the units funded in 1985 were incomplete. The MIS data and the PHA's comments were not considered in the rating process. The Richmond PHA's application was rated excellent in all factors and was funded for 50 units in July 1988. Consideration should have been given to the PHA's comments on the status of previously funded units.

As part of the application process, we believe PHAs should be required to report on the status of previously funded moderate rehabilitation projects. This information, which would help in evaluating the PHA's capabilities, should be used in the ranking process.

FY 1989 FUNDING PROCESS

On October 31, 1988, our staff met with Mr. Goldberger to review the process used to prepare recommendations for FY 1989 funding. We were advised that no actions were taken to revise the process or reassess applications. Many PHAs who were not funded in FY 1988 because of inconsistent treatment and/or lower scores were selected this round. Thus, Mr. Goldberger stated in an October 18, 1988 memo to Mr. Demery that the FY 1989 funding recommendations satisfied the OIG's concerns with the selection process.

Split Funding Applications

Before funding decisions were reached for FY 1989, the Assistant Secretary advised that 675 units were reserved for "split funded" applications. These units involve 7 PHAs that received some funding in FY 1988. We understand the reserved units will complete specific PHA projects partially funded in FY 1988. We examined the FY 1988 applications for the 7 PHAs. In 5 of the applications, there is no information that funds will be used for specific projects. These PHAs include:

Dade County
Michigan State HDA
Clark County
Santa Ana
L. A. County

It appears the Assistant Secretary may have obtained information outside the application process on which to base this decision.

Additional OIG Concerns

We currently are auditing over 20 PHAs in nine regions. Several of the PHAs audited received FY 1988 funding and were recommended for FY 1989 funding as well. Our audits point up significant deficiencies in the PHAs' administrative capability and/or their compliance with HUD requirements and their own Administrative Plans. In many cases, we provided copies of significant draft audit findings to Mr. Demery and Mr. Goldberger for review and comment. The following PHAs are in this category:

	88 Units	89 Units
Massachusetts EOCD	62	74
Richmond Redevelopment and Housing Agency	50	101
Maryland CDA	80	23
Michigan State Housing Development Agency	150	100

For example, MSHDA's operations were deficient in three specific areas that impact their administrative capability. On September 6, 1988, we provided copies of our draft report to Mr. Demery. That report discussed MSHDA's failure to assure that awards to developers complied with HUD requirements for open competition.

MSHDA did not assure that rental calculations were accurate and supportable. We estimated that rents under two contracts will be excessive by about $1.7 million over the 15 year contract terms.

MSHDA also approved units for moderate rehabilitation that were not occupied by income-eligible families contrary to HUD regulations.

In our discussion with Mr. Goldberger, he stated that our draft findings were not considered in the current funding decisions.

In other cases our reviews at PHAs haven't progressed to the point where the draft findings have been provided yet to the Office of Housing. However, the information developed to date is significant and our reports when issued will question various aspects of the PHAs' operations. Two PHAs exemplify this:

Dade County, Florida
Clark County, Nevada

More specifically for your information and consideration, our audits disclosed the following:

<u>Dade County</u>

The PHA has failed to comply with its Administrative Plan or with HUD regulations in awarding 17 projects to developers over the past several years. Virtually no competition occurs. Rather, the PHA selects developers based on their providing a HUD Form 185.

The PHA did not obtain and review developer cost certifications before executing HAP contracts in 16 of 17 contracts reviewed. A more detailed review of 6 projects showed excess payments made to owners exceed $94,000 at June 30, 1988. We estimate that, if not corrected, the excess rents will exceed $1.25 million over the 15 year term.

The PHA did not comply with HUD regulations pertaining to the determination of eligible tenants and units. As a result, the PHA has paid ineligible assistance on 33 units and 79 additional units are questionable because the PHA did not make a valid determination of eligibility.

<u>Clark County, Nevada</u>

The PHA advertised for units prior to receiving an allocation and selected a developer contingent upon receiving an allocation. The PHA did not readvertise when the actual funds were provided. At the time of the advertisement, the PHA had no Administrative Plan.

The PHA did not properly compute rents. We estimate that excess rents of over $5 million will be paid during the 15 year contract term if contract rents are not reduced.

The PHA did not properly determine unit eligibility in accord with HUD requirements. Rather they wrote to project tenants to inform them that if they did not meet income requirements, they must move from the project.

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In summary, we believe that the funding process used in July 1988 was flawed and not corrected in FY 1989. Moreover, the ultimate outcome of the process tends to perpetuate the perception of favoritism that the new procedures were designed to overcome. For these reasons I believe you need to move promptly to restore the integrity of the allocation process and to assure that the MRP is administered efficiently and effectively. To accomplish this, the recommendations made to the Secretary in my October 24, 1988 memorandum need to be addressed as soon as practicable.

Should you have questions or require additional information, please contact me.

cc: Thomas T. Demery, Assistant Secretary for
Housing-Federal Housing Commissioner, H