



Issue Date September 28, 2011

Audit Report Number 2011-PH-1016

TO: Donald J. Lavoy, Acting Deputy Assistant Secretary for Public and Indian Housing, Office of Field Operations, PQ
//signed//

FROM: John P. Buck, Regional Inspector General for Audit, Philadelphia Region, 3AGA

SUBJECT: The Philadelphia Housing Authority, Philadelphia, PA, Did Not Have Conflicts of Interest Related to Recovery Act Rehabilitation but Failed To Comply With Financial Disclosure Requirements

HIGHLIGHTS

What We Audited and Why

We audited the Philadelphia Housing Authority's compliance with the U.S. Department of Housing and Urban Development's (HUD) conflict-of-interest and financial disclosure requirements as a result of the Authority's initial failure to comply with an Office of Inspector General (OIG) subpoena during a previous American Recovery and Reinvestment Act of 2009 audit.¹ This audit was needed to evaluate information we later obtained from the Authority as a result of the United States District Court's summary enforcement of the subpoena. The audit objective addressed in this report was to determine whether there were any apparent conflicts of interest involving responsible Authority employees and contractors that performed Recovery Act-funded rehabilitation of the Authority's scattered site housing units and whether the Authority complied with mandatory financial disclosure reporting requirements.

¹ HUD OIG audit report number 2011-PH-1010, "The Philadelphia Housing Authority, Philadelphia, PA, Failed To Support Payments and Improperly Used Funds From the American Recovery and Reinvestment Act of 2009," dated May 17, 2011

What We Found

The information we obtained from enforcement of the OIG subpoena did not indicate the existence of any apparent conflicts of interest involving Authority employees and the contractor or subcontractors that completed Recovery Act-funded rehabilitation of the Authority's scattered site housing units. The audit did show, however, that the Authority did not comply with provisions in its Moving to Work Demonstration program agreement with HUD that required it to comply with State and local laws because it failed to comply with financial disclosure provisions in the Pennsylvania Public Official and Employee Ethics Act.

The Authority's new leadership took immediate corrective action during the audit to develop policies and procedures to address the problems noted. The Authority provided a copy of its proposed financial disclosure statement policies and procedures, which its board approved on July 22, 2011.² The policies and procedures were comprehensive and if implemented and enforced, should correct the problem.

What We Recommend

We recommend that HUD require the Authority (1) take immediate action to ensure that appropriate employees and board members file the required financial disclosures for calendar year 2010 and for the year following their termination of service and (2) fully implement and enforce the financial disclosure statement policies and procedures approved by its board on July 22, 2011.

For each recommendation in the body of the report 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 discussed the audit results with the Authority during the audit. We provided our draft audit report to the Authority on September 7, 2011, and requested its response by September 21, 2011. The Authority waived an exit conference and provided written comments to our draft report on September 21, 2011. It agreed with the finding in the report and stated that it would implement and enforce policies and procedures that it developed to address the finding and ensure its ongoing compliance. The complete text of the Authority's response can be found in appendix A of this report.

² Estelle Richman served as the sole member of the Authority's board of commissioners.

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BACKGROUND AND OBJECTIVE

The U.S. Housing Act of 1937 initiated the Nation's public housing program. That same year, the City of Philadelphia established the Philadelphia Housing Authority under Pennsylvania laws to address housing issues affecting low-income persons. The Authority's executive director at the beginning of the audit period was Carl R. Greene. The board of commissioners terminated Mr. Greene's employment, effective September 23, 2010, and hired Mr. Michael P. Kelly to serve as interim executive director, effective December 6, 2010. On August 8, 2011, Mr. Kelly began serving as the Authority's permanent executive director. Between the termination of Mr. Greene's employment and the hiring of Mr. Kelly, three assistant executive directors managed the day-to-day operations of the Authority. The Authority's main administrative office is located at 12 South 23rd Street, Philadelphia, PA.

Before March 4, 2011, a five-member board of commissioners governed the Authority. On March 4, 2011, the Authority's commissioners announced their resignations, and the U.S. Department of Housing and Urban Development (HUD) took control of the Authority. HUD Secretary Shaun Donovan appointed HUD's Chief Operating Officer, Estelle Richman, to serve as the sole member of the Authority's board and Michael P. Kelly as HUD's administrative receiver. The cooperative endeavor agreement formalizing HUD's takeover of the Authority expires on March 4, 2012, and is renewable in 1-year increments thereafter or until the Deputy Secretary and the mayor of Philadelphia mutually determine that the Authority has built sufficient capacity to be self-supporting.

The Authority is the Nation's fourth largest public housing authority and owns and operates more than 14,000 affordable housing units, serving about 81,000 people in Philadelphia. The Authority employs 1,200 people and has an annual budget of approximately \$345 million. It receives most of its funding from HUD. A small part of the budget (\$20 million) is received in the form of grants, notably the HOPE VI program to replace old developments. The Authority reports that another \$2 million is from interest and other forms of income and that it collects approximately \$13 million in rents.

In 1996, Congress authorized the Moving to Work Demonstration program as a HUD demonstration program. This program allowed certain housing authorities to design and test ways to promote self-sufficiency among assisted households, achieve programmatic efficiency, reduce costs, and increase housing choice for low-income households. Congress exempted participating housing authorities from much of the Housing Act of 1937 and associated regulations as outlined in the Moving to Work agreements. Participating housing authorities have considerable flexibility in determining how to use Federal funds. In December 2000, the Authority submitted an application to HUD to enter the program, and in February 2002, HUD signed a 7-year agreement with the Authority that was retroactive to April 2001. From April to October 2008, the Authority continued to operate under a HUD-developed plan to transition to traditional HUD program regulations because the term of its Moving to Work agreement had expired. In October 2008, HUD entered into a new 10-year Moving to Work agreement with the Authority. The expiration date of the Authority's new agreement is March 2018.

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009. This legislation included a \$4 billion appropriation of capital funds to carry out capital and management activities for public housing agencies as authorized under Section 9 of the United States Housing Act of 1937. The Recovery Act required that \$3 billion of these funds be distributed as formula grants and the remaining \$1 billion be distributed through a competitive process. Transparency and accountability were critical priorities in the funding and implementation of the Recovery Act. Overall, the Authority received \$126.5 million in Recovery Act capital funds, which was the largest amount of this funding awarded in HUD's Region III.³

HUD's Office of Public and Indian Housing Notice PIH 2010-34 provided public housing agencies and HUD field offices with information and procedures for the implementation of Public Housing Capital Fund Recovery competition grants as authorized by the Recovery Act. Section VI regarding procurement states that housing authorities shall continue to follow all 24 CFR (Code of Federal Regulations) Part 85 requirements regarding conflicts of interest, contract cost, and price. The Authority's Moving to Work agreement also required it to follow 24 CFR Part 85, which prohibits conflicts of interest. Additionally, the Authority's consolidated annual contributions contract with HUD prohibited it from entering into any contract or arrangement in connection with any project under the contract in which several classes of people had an interest, direct and indirect, during their tenure or for 1 year thereafter. These classes included any present or former member or officer of the governing body of the Authority, any Authority employee who formulated policy or influenced decisions with respect to the project(s), and any public official who exercised functions or responsibilities with respect to the project(s) or the Authority.

The audit objective addressed in this report was to determine whether there were any apparent conflicts of interest involving responsible Authority employees and contractors that performed Recovery Act-funded rehabilitation of the Authority's scattered site housing units and whether the Authority complied with mandatory financial disclosure reporting requirements.

³ Region 3 encompasses Pennsylvania, Virginia, Maryland, West Virginia, Delaware, and the District of Columbia.

RESULTS OF AUDIT

Finding: The Authority Did Not Have Conflicts of Interest Related to Recovery Act Rehabilitation but Failed To Comply With Financial Disclosure Requirements

We did not identify any evidence of apparent conflicts of interest with 28 Authority employees⁴ who we determined could influence the awarding and management oversight of the Authority's contract and subcontracts for rehabilitation of its scattered site units. The Authority did not comply, however, with provisions in its Moving to Work agreement with HUD that required it to comply with State and local laws because it failed to comply with financial disclosure provisions in the Pennsylvania Public Official and Employee Ethics Act. The Authority's new leadership took immediate corrective action during the audit to develop policies and procedures and began to address the problems noted. The Authority provided us a copy of its proposed financial disclosure statement policies and procedures, which were approved by its board² on July 22, 2011. The procedures were comprehensive and if implemented and enforced, should correct the problem.

Conflicts of Interest Related to Recovery Act Rehabilitation Were Not Evident

Transparency and accountability were critical priorities in the funding and implementation of the Recovery Act. In keeping with these priorities, we asked the Authority to provide partial Social Security numbers for 28 of its employees to perform routine audit tests to review for the existence of apparent conflicts of interest during our recent Recovery Act Capital Fund audit.¹ The Authority, through its outside law firms of Schnader, Harrison, Segal & Lewis, LLP, and Ballard Spahr Andrews & Ingersoll, LLP, refused to provide the requested partial Social Security numbers. Therefore, the Office of Inspector General (OIG) served the former executive director with a subpoena on July 14, 2010, to obtain the information. The Authority, through its outside counsel, contested the OIG subpoena in United States District Court. On February 4, 2011, the United States District Court for the Eastern District of Pennsylvania ordered summary enforcement of the subpoena on behalf of OIG. The Authority complied with the court order and provided the requested partial Social Security numbers on February 14, 2011.

⁴ This review did not include the Authority's former board of commissioners.

We reviewed information pertaining to the 28 Authority employees⁴ who we determined could influence the awarding and management oversight of the Authority's contract and subcontracts for rehabilitation of its scattered site units and found no evidence of apparent conflicts of interest with those employees.

The Authority Did Not Comply With State Financial Disclosure Requirements

Section 1.C. of the Authority's Moving to Work agreement with HUD, as amended, required the Authority to comply with State and local laws. The Authority's employees and its board of commissioners were subject to conflict-of-interest provisions and financial disclosure reporting under the Ethics Act. The Act required them to complete and file a statement of financial interests for each year in which they held the position and for the year following their termination of that service. The Authority's records showed that 45 of its employees and 3 members of its board of commissioners filed 109 annual financial disclosures between 2007 and 2010. However, we identified 27 additional employees, who were required under the Ethics Act to file disclosures based on their positions, who did not do so. Additionally, we reviewed the 109 financial disclosures filed by the 45 Authority employees and 3 members of the board of commissioners for calendar years 2007, 2008, 2009, and 2010 and found many deficiencies with the disclosures.⁵

- ✓ 68 were not filed on time;
- ✓ 61 were incomplete or missing direct or indirect sources of income;
- ✓ 26 were incorrect or missing the year;
- ✓ 19 were inaccurate or missing the governmental entity;
- ✓ 17 were incomplete, inaccurate, or missing the public office;
- ✓ 6 were inaccurate or incomplete;
- ✓ 4 were undated; and
- ✓ 4 were missing the occupation or profession.

The Former Board Did Not Comply With State Financial Disclosure Requirements

Former members of the Authority's board of commissioners did not file financial disclosure statements as required by the Ethics Act. Authority officials informed us that in years 2008, 2009, and 2010, they notified the five board members that they were required to file financial disclosure statements for the prior calendar year. However, the Authority was unable to provide disclosures filed by two board members for those years. One of the two board members also served as a

⁵ Of the 109 financial disclosure forms reviewed, 65 contained multiple deficiencies.

member of the Philadelphia City Council during those years.⁶ The Authority provided disclosures that were filed with the Authority by three of five board members, but the disclosures filed by two of the three for each of the 3 years were dated September 23, 2010, well beyond the filing deadlines.⁷ The third board member was the former board chairman. His 2009 disclosure and a disclosure that did not note the reporting year were also dated September 23, 2010, and his 2007 disclosure was not dated.

The Authority Lacked Adequate Financial Disclosure Policies and Procedures

HUD regulations at 24 CFR (Code of Federal Regulations) 85.36(b)(3) require grantees to maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. HUD Handbook 7460.8, REV-2, chapter 4, explains the specific ethical requirements for a public housing authority's contracting under HUD regulations. Additionally, section 1.C. of the Authority's Moving to Work agreement with HUD, as amended, required the Authority to comply with State and local laws. However, the Authority's policies and procedures were not adequate to ensure that it complied with HUD regulations and its Moving to Work agreement related to financial disclosures.

The Authority's New Leadership Took Corrective Action

The Authority's new leadership took immediate corrective action during the audit to develop financial disclosure statement policies and procedures. The Authority's board² passed a resolution to approve the procedures on July 22, 2011. We reviewed the policies and procedures and determined that they were comprehensive and would adequately address the deficiencies noted during the audit if the Authority implements and enforces them. The Authority also told us during the audit that it would take immediate action to ensure that appropriate employees file the required disclosures for calendar year 2010.

⁶ Local public officials are required to file a disclosure with the governing authority of the respective local political subdivision. However, when serving in multiple capacities, a copy of the form is required to be filed with each entity.

⁷ Disclosures are due no later than May 1 of each year a position is held and of the year after leaving the position.

Recommendations

We recommend that the Acting Deputy Assistant Secretary for Public and Indian Housing, Office of Field Operations, direct the Authority to

- 1A. Take immediate action to ensure that appropriate employees and board members file the required financial disclosures for calendar year 2010 and for the year following their termination of service if applicable.
- 1B. Fully implement and enforce the financial disclosure statement policies and procedures approved by its board on July 22, 2011.

SCOPE AND METHODOLOGY

We performed our audit work from March through August 2011 at the Authority's offices located at 12 South 23rd Street, Philadelphia, PA, and at our office located in Philadelphia, PA. The audit covered the period April 2008 through February 2011 but was expanded when necessary to include other periods. We relied in part on computer-processed data in the Authority's computer system. Although we did not perform a detailed assessment of the reliability of the data, we did perform a minimal level of testing and found the data to be adequate for our purposes.

To accomplish our objective, we reviewed

- Applicable laws, regulations, the Authority's procurement policy, the Authority's Moving to Work agreement and amendments, the Authority's Human Resources Manual, employee position descriptions, HUD program requirements at 24 CFR Part 85, HUD Handbook 7460.8, REV-2, the Pennsylvania Procurement Code, and the Pennsylvania Public Official and Employee Ethics Act.
- The Authority's employee and contract listings, computerized database information from public sources including personal and contractor data, organizational chart, board meeting minutes, policies and procedures, and consolidated annual contributions contract.

We interviewed Authority officials involved with the oversight of employee financial disclosure statement filings.

We identified 28 Authority personnel of interest based on information that the Authority provided during our recently completed audit of its use of Recovery Act funds for its public housing scattered site units.¹ We determined that they were in a position to influence the award of the Authority's contract for rehabilitation of its scattered site units or the oversight and management of the contract. We also identified 35 principal employees of the contracting firm and its subcontractors based on a list provided by the Authority and supplemented by our research of the firms through Dunn & Bradstreet, Lexis/Nexis, Experian, and the Pennsylvania registered corporation databases. Using the Lexis/Nexis public records search, we further identified household members of each Authority and contractor or subcontractor employee in our selection. We also identified potential relatives, neighbors, and other associates for each of the individuals in our selection and for each of their household members. We arrived at a database containing a total of 5,037 individuals. We analyzed the database using computer-aided audit tools to determine whether there was any commonality between or among the individuals which would give us reason to believe an apparent conflict of interest existed.

We reviewed all statement of financial interest forms filed by Authority employees and members of the Authority's board of commissioners for calendar years 2007, 2008, 2009, and 2010 and all requests for approval of outside employment forms filed with the Authority by 25 of the 28 employees on our list.

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 a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

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

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls 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:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- The Authority lacked adequate policies and procedures to ensure its compliance with provisions in its Moving to Work agreement with HUD that required it to comply with State and local laws.

Appendix A

AUDITEE COMMENTS

Philadelphia Housing Authority
Building Beyond Expectations

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September 12, 2011

Mr. John P. Buck
Regional Inspector General for Audit
Philadelphia Region
U.S. Department of Housing and Urban Development
100 Penn Square East
Philadelphia, PA 19107-3380

Re: Review of PHA's Conflict of Interest and Financial Disclosure Requirements

Dear Mr. Buck:

The Philadelphia Housing Authority ("PHA") is in receipt of the draft audit report regarding the U.S. Department of Housing and Urban Development's (HUD) review of the PHA's conflict of interest and financial disclosure requirements.

The PHA is pleased that your review did not find "any evidence of apparent conflicts of interests" with the 28 employees your audit examined. Although your review found that the PHA did not comply with the Pennsylvania Public Official and Ethics Act ("Ethics Act"), I am pleased that the report recognizes that the new PHA management took immediate corrective action during your review to develop policies and procedures to address the deficiency noted in the report. The PHA is committed to ensuring its ongoing compliance with all laws, rules and regulations; and is actively working to develop internal controls that, when implemented and adhered to, will guarantee PHA's compliance.

As your draft report notes, during the course of your audit the PHA took immediate steps to address its employees' non-compliance with the Ethics Act. Based on guidance provided by the State Ethics Commission for the 2010 reporting year, the PHA identified all employees subject to the Ethics Act filing requirement. In February 2011, the PHA notified subject employees of their obligation to file their annual Statement of Financial Interest form, which the PHA included in its notification. In April 2011, the PHA issued a follow-up letter to staff reminding them of the requirement to file their completed Statement of Financial Interest forms no later than May 1, 2011. Indeed, the PHA's efforts to ensure its employees' compliance with the Ethics Act were largely successful: all current employees subject to the ethics act filing requirement have completed their 2010 filing.

Notwithstanding the PHA's efforts, however, nine (9) former employees/officers, including members of the former Board of Commissioners, failed to submit the required disclosures. Accordingly, the PHA will refer these former employees/officers to the State Ethics Commission for any enforcement action it deems appropriate.

As your draft report notes, in July 2011, the PHA's Board of Commissioners approved new financial disclosures policies and procedures. Like you, we believe that the policies and procedures developed are comprehensive, which the PHA intends to aggressively enforce.

Accordingly, the PHA's Office of Audit and Compliance ("OAC") will conduct annual reviews of PHA staff financial disclosures to ensure that staff fully complies with the Ethics Act filing requirements.

Additionally, as part of the PHA's ongoing commitment to compliance, the Authority has developed several policies and procedures aimed at not only at ensuring the PHA ongoing compliance but also transparency and accountability. To date, the PHA has developed and will implement policies/procedures and operational changes in the following areas (to name a few):

1. **Standards of Ethical Conduct**—In September 2011, the PHA will seek Board approval of its new Standard of Ethical Conduct policy. This new comprehensive policy, the first of its kind for the PHA, outlines principles for ethical conduct and requires that PHA employees and contractors report conflicts of interest, unethical or questionable conduct to the PHA's OAC;
2. **Anti-Fraud Policy**—In September 2011, the PHA, with the approval of its Board, will adopt a more stringent anti-fraud policy. This new policy puts an affirmative obligation on PHA employees, contractors and clients to report fraud, corruption and other unethical or questionable activities involving PHA employees, contractors and tenants. Further, the new policy provides whistle blower protection for employees who file bona fide complaints and prohibits retaliation against employees for filing complaints;
3. **Equal Employment Opportunity ("EEO")**—PHA has adopted a zero tolerance EEO policy and procedure aimed at ensuring, among other things, that we create workplace free from discrimination, sexual harassment, retaliation; and where individuals have equal opportunity to PHA jobs, contracts and programs;
4. **Outside Employment**—The PHA has developed a policy governing PHA employees who engage in outside employment. This new policy requires employees to seek approval for non-PHA employment. The policy prohibits employees from engaging out outside employment activities that would be a conflict of interest with their PHA employment. Specifically, the policy bars employees from working for any PHA contractor or resident;

5. **Appointment of PHA's Ethics Officer**—Pursuant to a Board resolution in March 2011, the PHA's General Counsel assumed responsibilities as the PHA's Ethics Officer. In this role, the General Counsel responds to employees' questions and provides guidance to staff on ethics issues; and
6. **Officer of Audit and Compliance**—Pursuant to a Board resolution in January 2011, the PHA established its Office of Audit and Compliance. Currently, the OAC has three functional areas: compliance, internal audit and investigations. The ongoing consolidation of the OAC further signifies the PHA's intent to be in full compliance with all applicable policies, rules and regulations.

The above-referenced policies represent a small sampling of new policies and procedures being adopted by the PHA. Beginning in October 2011, all PHA employees will be required to attend mandatory training on these and other new policies and procedures, and employees will be required to acknowledge their receipt of these policies.

On behalf of the PHA management and staff, thank you for your review and your assistance. We look forward to working cooperatively with you and your colleagues to address all your concerns and to correct any deficiency highlighted by your audits.

Please do not hesitate to contact me at (215) 684-4025, should you have any questions or concerns regarding this matter.

Sincerely yours,

Kelvin A. Jeremiah
Director, Office of Audit and Compliance

cc: Estelle Richman, Commissioner
Michael Kelly, Executive Director/Administrative Receiver
Dennis Bellingtier, Director, Office of Public Housing
Janea Jordon, Deputy Director, Office of Audit and Compliance
Audrey Lim, Acting Director of Human Resources
Nnena Ukwa, Internal Audit Manager