



Housing Authority of the City of Los
Angeles,
Los Angeles, CA
Rental Assistance Demonstration Program

Office of Audit, Region 9
Los Angeles, CA

Audit Report Number: 2018-LA-1007
August 24, 2018



To: Thomas R. Davis, Director, Office of Recapitalization, HTR
Marcie P. Chavez, Director, Office of Public Housing, Los Angeles, CA, 9DPH
//SIGNED//

From: Tanya E. Schulze, Regional Inspector General for Audit, 9DGA

Subject: The Housing Authority of the City of Los Angeles, CA, Generally Administered
Its Rental Assistance Demonstration in Accordance With HUD Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Housing Authority of the City of Los Angeles' Rental Assistance Demonstration conversion.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG website. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 213-534-2471.



Audit Report Number: 2018-LA-1007

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The Housing Authority of the City of Los Angeles, CA, Generally Administered Its Rental Assistance Demonstration in Accordance With HUD Requirements

Highlights

What We Audited and Why

We audited the Housing Authority of the City of Los Angeles' Rental Assistance Demonstration (RAD) conversion to the Section 8 Project-Based Voucher Program. We selected the Authority because review of RAD conversions was aligned with the goals of our annual audit plan and the Authority's conversion included previously environmentally toxic land that was recently remediated. The objective of our review was to determine whether the Authority administered its RAD conversion projects in accordance with applicable HUD requirements. Specifically, we wanted to determine whether the Authority (1) executed appropriate written agreements, (2) ensured that project financing sources were secured, (3) ensured that the required environmental reviews were accomplished, (4) maintained separate books and records for the RAD conversion, (5) spent HUD funds for eligible and reasonable purposes, (6) followed occupancy requirements, and (7) obtained a capital needs assessment.

What We Found

The Authority generally complied with RAD program requirements in the areas that we were able to fully review. However, since the Authority's conversions were in progress, we could not make a full assessment for all RAD program requirements.

What We Recommend

This report contains no recommendations.

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Background and Objective

The Housing Authority of the City of Los Angeles was established in 1938 by the City of Los Angeles and has an annual budget of more than \$1 billion. The Authority's funds come from five main sources: HUD's annual operating subsidy, HUD's annual Public Housing Capital Fund, Section 8 administrative fees, and rent from public housing residents, plus other program and capital grants from various sources.

The Authority's strategic mission is to preserve its existing affordable housing supply of more than 83,000 units, while ensuring that the units are both safe and clean. The Authority works collaboratively with residents and public, nonprofit, and private entities to create viable, healthy communities and to empower able residents to achieve financial independence.

The Rental Assistance Demonstration program (RAD) was authorized by the Consolidated and Further Continuing Appropriations Act of 2012 and has two separate components:

- The First component allows projects funded under the public housing program to convert their assistance to long-term, project-based Section 8 rental assistance contracts. Under this component of RAD, public housing agencies may choose between two forms of Section 8 housing assistance payments contracts: project-based vouchers or project-based rental assistance.
- The Second component allows owners of projects funded under the Rent Supplement, Rental Assistance, and Mod Rehab programs to convert tenant protection vouchers to project-based vouchers or project-based rental assistance upon contract expiration or termination occurring after October 1, 2006.

RAD provides the opportunity for public housing agencies to test the conversion of public housing and other HUD-assisted properties to long-term, project-based Section 8 rental assistance properties to achieve certain goals, including the preservation and improvement of these properties through enabling access by public housing agencies and owners to private debt and equity to address immediate and long-term capital needs. RAD is also designed to test the extent to which residents have increased housing choices after the conversion and the overall impact on the subject properties.

The Authority received its commitments to enter into housing assistance payments contracts between August 2014 and October 2017. It began converting a total of 297 units from its Ramona Gardens¹ and Jordan Downs public housing projects to project-based voucher RAD and other affordable units. The Jordan Downs RAD project consists of 106 units converting to RAD and an additional 180 affordable apartments, including Section 8 project based voucher, tax credit only,

¹ The RAD conversion will take place at the Rose Hill Courts development, which is administered by the Ramona Gardens public housing project.

and manager units. The projects total more than \$133 million in estimated development costs, and there are plans to ultimately replace all 713 units in the development. As of May 2018, the Authority had closed one project with construction in progress. The remaining three were open and were in various stages of the conversion process. During the course of our review, the Authority closed an additional project, with two remaining in an open status. The table below lists the RAD conversion projects, estimated development cost, and status.

	Project	Estimated development cost	Status
1	Ramona Gardens	\$50,029,160	Open
	Subtotal	50,029,160	
2	Jordan Downs 1A	59,471,678	Closed
3	Jordan Downs 1B	73,972,060	Closed
4	Jordan Downs MP3*	0	Open
5	Jordan Downs MP4*	0	Open
	Subtotal	133,443,738	
	Total	183,472,898	

*No estimated development costs were available.

Our objective was to determine whether the Authority administered its RAD conversion projects in accordance with applicable HUD requirements. Specifically, we wanted to determine whether the Authority (1) executed appropriate written agreements, (2) ensured that project financing sources were secured, (3) ensured that the required environmental reviews were accomplished, (4) maintained separate books and records for the RAD conversion, (5) spent HUD funds for eligible and reasonable purposes, (6) followed occupancy requirements, and (7) obtained a physical conditions assessment.

Results of Audit

Finding: The Authority Generally Administered Its Rental Assistance Demonstration Conversions in Accordance With HUD Program Requirements

The Authority generally administered its RAD conversion in accordance with HUD requirements. Specifically, the Authority ensured that it (1) executed proper written agreements, (2) secured project financing sources, (3) completed required environmental reviews, (4) spent HUD funds for eligible and reasonable purposes, (5) generally complied with HUD occupancy requirements, and (6) completed a capital needs assessment to determine short-term rehabilitation and long-term capital needs. We could not fully evaluate all areas intended for review because the conversion process was ongoing for all of the projects and a number of requirements were not yet required to be performed or complete.

Written Agreements Were Properly Executed

For Jordan Downs 1A,² the Authority had written agreements, which ensured that HUD's interest in the program units was protected as required by HUD Office of Public and Indian Housing (PIH) Notice PIH-2012-32 (REV-3).³ The Authority established a use agreement, which included the necessary provisions to ensure that the agreement would be superior to all liens on the property, run for the same term as the initial housing assistance payments contract, automatically renew upon extension or renewal of the contract, and remain in effect even in the case of abatement or termination of the contract. The Authority's agreement also provided appropriate provisions in the event that the housing assistance payments contract was removed due to breach, noncompliance, or insufficiency of appropriations. The Authority also established a ground lease agreement to further protect its interests.

² The other three Jordan Downs conversions (1B, MP3, and MP4) did not have an agreement in place due to the early status of their conversions.

³ Notice PIH-2012-32 (REV-3), paragraph 1.6(B)(4), states that covered projects must have an initial RAD use agreement that will (1) be recorded superior to all liens on the property; (2) run for the same term as the initial housing assistance payments contract, automatically renew upon extension or renewal of the contract for a term that coincides with the renewal term of the contract, and remain in effect even in the case of abatement or termination of the contract (for the term the contract would have run, absent the abatement or termination), unless the HUD Secretary approves termination in the case of a transfer of a assistance; (3) in case of breach, noncompliance, or insufficient appropriations, provide that new tenants have incomes at or below 80 percent of area median income and rents that do not exceed 30 percent of 80 percent of area median income for the remainder of the term of the agreement; and (4) require compliance with all fair housing and civil rights requirements.

Financing Sources Were Secured

The Authority's financing plans for Jordan Downs 1A and 1B⁴ generally met the requirements outlined in Notice PIH-2012-32 (REV-3).^{5,6} We reviewed the Authority's financing letters, source of funds, and plans for the use of funds and determined that the financing sources for Jordan Downs 1A were properly secured and that financing sources for Jordan Downs 1B were also obtained but were being finalized at the time of our review. Financing sources were identified in the Authority's RAD application and generally included the key terms required by the Notice. The Authority used mainly secondary financing, 4 percent low-income housing tax credits, State and local funds, and the Authority's own internal funding to fund the conversions.

Environmental Requirements Were Met

The Authority obtained the necessary environmental reviews and certifications⁷ to ensure that no environmental issues would impact the Jordan Downs 1A and 1B conversions.⁸ No problems were noted, and reviewing officials determined that no further action was required. In addition, we did not find evidence that any environmental remediation costs were charged to any of the four projects.

HUD Funds Were Used for Eligible and Reasonable Purposes

For Jordan Downs 1A, we verified that the Authority spent \$5 million in HUD replacement housing factor funds for eligible and reasonable purposes.⁹ The funds were spent on eligible escrow, construction, and development costs. We took no issue with the Authority's payment of

⁴ Jordan Downs projects MP3 and MP4 were still in the early stages, and financial plans were, therefore, not yet available or required to be complete.

⁵ Notice PIH-2012-32 (REV-3), attachment 1A, paragraph H, states that for each proposed loan, equity contribution, or grant, the public housing agency must include (1) a recent lender, investor, or grant engagement letter, dated no later than 60 days after the financing plan submission, with key terms identified (including amount, repayment terms, interest rate, amortization, maturity, prepayment restrictions, pay-in schedule, etc.) from all financing provider(s) (key terms for permanent financing must comply with conditions in paragraph 1.4(B)(1) of the Notice); (2) a brief discussion of conditions or milestones to be satisfied before closing; (3) documentation showing that the first mortgage lender has consented to the use agreement and that the lien of the new first mortgage loan will be subordinate to the use agreement; and (4) an estimated projected closing date for all proposed financing.

⁶ Notice PIH-2012-32 (REV-3), paragraph 1.4(B)(1), requires permanent debt financing on covered projects to be at a fixed rate of interest, for a fixed term, fully amortized over no more than 40 years, and with a maturity date or balloon of not earlier than 18 years, except in the case of project-based voucher conversions when the contract is for less than 18 years, in which case the maturity date or balloon cannot be less than the term of the contract.

⁷ Notice PIH-2012-32 (REV-3), paragraph 1.4(A)(3), requires that proposed RAD projects receive environmental review under either 24 CFR (Code of Federal Regulations) Part 50 or Part 58, as applicable, and environmental documents be submitted as a part of the applicant's financing plan.

⁸ Environmental reviews were not available or due for Jordan Downs MP3 and MP4 during our fieldwork due to the early stages of the projects.

⁹ Notice PIH-2012-32 (REV-3), paragraph 1.5(A), states that public housing agencies are permitted under RAD to use available public housing funding, including operating reserves, capital funds, and replacement housing factor funds, and demolition and disposition transitional funding as a source of capital in the development budget to support conversion, whether for rehabilitation or new construction, as well as to increase initial contract rents. Eligible conversion-related uses for these funds include predevelopment, development, or rehabilitation costs of the covered project.

predevelopment expenses and verified that no HUD funds had been spent for the remaining projects.

HUD Occupancy Requirements Were Generally Followed

The Authority held the required meetings to inform residents of the upcoming RAD conversions and address questions from tenants. Public housing agencies are required to notify residents of the proposed RAD conversion, conduct meetings, and prepare written responses to any comments received.¹⁰ The meetings were slightly delayed for Jordan Downs 1A and 1B, but HUD was notified and they had taken place. Documentation was also provided showing that later meetings were held to discuss the remaining conversion phases, provide redevelopment updates, and discuss associated relocation planning.

Some Areas Could Not Be Fully Evaluated

Due to the ongoing status of the conversions (see the Background and Objective section), a number of requirements were not yet required to be performed or completed. Therefore, we could not fully evaluate several areas intended for review at the Jordan Downs sample projects. We could not determine whether the Authority maintained separate books and records from the RAD owner because the properties were not complete; therefore, no applicable housing assistance payments contracts had been established. In addition, the Authority's action on its waiting list and developer fees could not be fully assessed. Development of the waiting list was underway during the course of our review for Jordan Downs 1A and 1B, and all developer fees had not been finalized and paid for Jordan Downs 1A. Finally, the Authority completed the required capital needs assessment for Jordan Downs 1A and 1B. However, we could not compare the work identified in the assessment to completed work because construction is not yet complete.

Conclusion

The Authority generally administered its RAD conversion in accordance with HUD requirements. Specifically, the Authority ensured that it executed proper written agreements, secured project financing sources, completed required environmental reviews, spent HUD funds for eligible and reasonable purposes, and generally complied with HUD occupancy requirements. However, we could not fully evaluate all areas intended for review because the conversion process was ongoing for all of the projects.

Recommendations

This report contains no recommendations.

¹⁰ Notice PIH-2012-32 (REV-3), section 1.8, requires the public housing agency to (1) notify residents of projects proposed for conversion and legitimate resident organizations of the agency's intent to pursue a conversion; (2) conduct at least two meetings with residents of projects proposed for conversion to discuss conversion plans and provide an opportunity for comment; (3) before the two meetings, issue a RAD information notice to inform residents about proposed projects and to inform them of their rights; and (4) prepare written responses to comments received from residents to be submitted with the RAD application.

Scope and Methodology

We performed our audit work at the Authority located at 2600 Wilshire Boulevard, Los Angeles, CA, from March to May 2018. Our review generally covered the period January 2014 through May 2018.

To accomplish our objective, we performed the following:

- Reviewed HUD regulations and requirements.
- Interviewed appropriate HUD and Authority personnel.
- Reviewed the Authority's policies, procedures, and controls.
- Reviewed HUD monitoring reports.
- Reviewed status reports from HUD's RAD Resource Desk¹¹.
- Conducted a site visit to the Jordan Downs redevelopment.
- Reviewed and analyzed supporting documents, including financing plans, written agreements, and program expenditures.

The audit universe consisted of five projects with an estimated total development cost of more than \$183.4 million. For our survey, we selected four projects totaling more than \$133.4 million from the Jordan Downs redevelopment for review. Our survey items represented 73 percent of the total estimated development cost for the five RAD conversion projects initiated by the Authority.

We used a nonstatistical sample selection for our review because our audit universe consisted of a small number of projects. We did not perform a 100 percent review due to resource constraints. We selected a sample of the four Jordan Downs projects in our universe (1A, 1B, MP3, and MP4) because the site included land that was recently environmentally remediated. Since the sampled project conversions were in progress at varying stages, our review was limited to evaluating requirements that should have been completed for each project at the time of our fieldwork. Therefore, our audit results were limited to the projects in our sample and cannot be projected to the universe.

¹¹ The RAD Online Resource Desk serves as a comprehensive information archive enabling searches of all published guidance on the Rental Assistance Demonstration. The Desk also serves as the main portal for Demonstration participants to ask questions, search for information and forms, upload documents, and track their progress toward closing. Access is available to the public as well as HUD employees and public housing agency staff.

Our conclusions were based primarily on supporting documentation obtained during the audit. However, we used reporting data from HUD's RAD Resource Desk to verify information in the source documentation received from the Authority and to obtain needed background information. The reporting data were consistent with the information contained in the source documents. Therefore, the data were sufficiently reliable for our use during the audit.

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(s). 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:

- Effectiveness and efficiency of program operations – Implementation of policies and procedures to ensure that program funds are used for eligible purposes.
- Relevance and reliability of information – Policies and procedures that management has implemented to reasonably ensure that operational and financial information used for decision making and reporting externally is relevant, reliable, and fairly disclosed in reports.
- Compliance with applicable laws and regulations – Implementation of policies and procedures to ensure compliance with applicable HUD rules and requirements.

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.

We evaluated the internal controls related to our audit objective in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance regarding the effectiveness of the internal control structure as a whole. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

Appendixes

Appendix A

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments



HOUSING AUTHORITY OF THE CITY OF LOS ANGELES
AN EQUAL EMPLOYMENT OPPORTUNITY - AFFIRMATIVE ACTION EMPLOYER
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PRESIDENT AND CEO
DOUGLAS GUTHRIE

Via Email only
August 8, 2018

Office of Inspector General
Office of Audit, Region 9
Attn: Tanya E. Schulze, Regional Inspector General for Audit

RE: HUD OIG Audit of HACLA's Rental Assistance Demonstration program

Dear Ms. Schulze:

The Housing Authority of the City of Los Angeles ("HACLA" or the "Authority") appreciates the opportunity to provide comments on the Office of Inspector General's ("OIG") draft Audit Report No. 2018- LA-XX (the "Report") that was emailed to HACLA on July 24, 2018.

HACLA acknowledges the conclusion that the Authority generally complied with the RAD program requirements in the areas that HUD OIG was able to fully review and considers this as a testament to its high caliber implementation of the RAD program.

HACLA would like to take this opportunity to respond to some of the minor discrepancies in the report and provide further clarification on these matters.

a. Reference to RAD Conversion at Ramona Gardens (Page 3)

HACLA is in the process of redeveloping the 100 unit Rose Hill Courts (RHC) public housing site. The Housing Authority had requested RAD assistance for 11 units at RHC with the balance of the property anticipated to undergo Section 18 Demolition/Disposition. Since Rose Hill is a small site, it is administered through the larger Ramona Gardens development (AMP CA004000401). HACLA does not have any current plans for conversion of Ramona Gardens at this point in time. Therefore, to prevent confusion to the readers of this report, HACLA requests that OIG replace references to Ramona Gardens with Rose Hills Courts, or in the alternative, include a footnote reference for Ramona Gardens stating "HACLA is planning to carry out a partial RAD conversion of the Rose Hill Courts development which is part of the Ramona Gardens AMP".

Comment 1

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 2

OIG Review of HACLA RAD Program
Page 2

b. Estimated Development Costs for the RAD Conversion projects

The statement on Page 3 that Jordan Downs RAD consists of four projects (106 units) totaling more than \$133 million in estimated development costs is erroneous since the RAD units being converted are a minor component of each of the four projects. Also, this sentence implies that these 106 units cost \$133 million or more than \$1.25 million per unit.

The following is the breakdown of the Jordan Downs 1A and 1B projects. These two projects have a total of 70 RAD units (32 units in 1A and 38 units in 1B) and comprise less than 24% of the overall 250 units being developed in the two projects. The 250 unit project is estimated to cost \$133 million at an average cost of \$533,775 per unit.

Project	Total Units	RAD units	Non-RAD Units (regular PBV, tax credit, manager unit)	Total Development Costs
Jordan Downs 1A	115	32	83	\$59,471,678
Jordan Downs 1B	135	38	97	\$73,972,060
Total	250	70	180	\$133,443,738

Therefore, please include a reference that the RAD conversions are being carried out within larger projects that include non-RAD Section 8 regular PBV units, tax credit only units, and manager units and make the necessary clarifications to the sentence.

c. Physical Conditions Assessments

The statement on Page 7 that no physical condition assessments can be conducted until the properties' construction is complete is incorrect. HACLA conducted RAD Physical Conditions Assessments (RPCA) for both the Jordan Downs 1A and Jordan Downs 1B projects in accordance with the RAD requirements in place at the time of their Financing Plan submissions. Since both projects are New Construction and Non-FHA Low Income Housing Tax Credit (LIHTC) transactions, only the RPCA tool was required to be completed. The RPCA tool is an Excel spreadsheet with various tabs to collect and analyze data on the proposed development. The information entered into the RPCA Tool, using the schedule of values provided by the general contractor & signed off by the developer, determines the amount of Initial Repairs or Scope of the Work for the New Construction and the Annual Deposit to Replacement Reserve. These outputs from the RPCA tool are included in the RAD Conversion Commitments (RCC) issued for both these properties.

HACLA had included the RPCA Excel tools and RCCs in its data submission to OIG for both Jordan Downs 1A and 1B.

Also, please note that HACLA will conduct Housing Quality Standard (HQS) inspections for all RAD and Section 8 HAP assisted units prior to occupancy and no later than the construction completion deadline as indicated in the RCC, to ensure compliance with HQS.

Comment 3

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

OIG Review of HACLA RAD Program
Page 3

HACLA would like to thank OIG staff for its cooperation and patience during the Audit. If you have any questions, please feel free to contact me at (213) 252-1810.

Sincerely,



 Douglas Guthrie
President and Chief Executive Officer

cc: Marcie Chavez, Director, Los Angeles Office of Public Housing, HUD
Rosanne Chavez, Deputy Director, Los Angeles Office of Public Housing, HUD
Thomas R. Davis, Director, Office of Recapitalization, HUD
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Kimberly R. Randall, Acting Assistant Inspector General for Audit, HUD

OIG Evaluation of Auditee Comments

- Comment 1 We added a footnote to clarify that the RAD conversion will take place at the Rose Hill Courts development, which is administered by the Ramona Gardens public housing project.
- Comment 2 Since the paragraph in question was intended to provide general background on all conversions currently in progress, we included the total number of units for the Ramona Gardens and Jordan Downs housing projects. We also added clarification that more than \$133 million in development costs included RAD and other affordable housing apartments consisting of Section 8 project based voucher, tax credit only, and manager units.
- Comment 3 We clarified that the Authority completed the required Capital Needs Assessments for Jordan Downs 1A and 1B. We also clarified that since the projects are still under construction, we could not compare work identified in the assessment to any completed work.