



Issue Date May 28, 2008

Audit Report Number 2008-LA-1010

TO: K.J. Brockington, Director, Los Angeles Office of Public Housing, 9DPH

Joan S. Hobbs

FROM: Joan S. Hobbs, Regional Inspector General for Audit, Region IX, 9DGA

SUBJECT: The Housing Authority of the City of San Buenaventura, San Buenaventura, California, Did Not Manage HUD Program Funds in Accordance with HUD Requirements

HIGHLIGHTS

What We Audited and Why

We audited the Housing Authority of the City of San Buenaventura (Authority) in response to a hotline complaint alleging mismanagement and misuse of U.S. Department of Housing and Urban Development (HUD) funding. Our overall audit objective was to determine whether the Authority's financial activities, operations, and controls complied with HUD requirements.

What We Found

The Authority stopped paying its Low Rent Public Housing program's Payment-in-Lieu of-Taxes obligations to the City of San Buenaventura (City) without City or HUD approval and used the associated HUD funds to acquire non-HUD-related property. Additionally, it used Low Rent Public Housing program funds to temporarily cover its Housing Choice Voucher program overspending for fiscal year 2007, placing both programs at risk.

What We Recommend

We recommend that HUD require the Authority to comply with HUD's requirements regarding the use of Payment-in-Lieu-of-Taxes funds, reimburse the Low Rent Public Housing program \$496,137 from nonfederal funds, and implement written procedures for the accounting and use of both Housing Choice Voucher and Low Rent Public Housing program funds.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided the Authority with a discussion draft report on April 21, 2008, and held an exit conference with the Authority's officials on May 5, 2008. The Authority also provided written comments on May 5, 2008. It generally disagreed with our report findings.

The complete text of the auditee's response without the voluminous attachments, along with our evaluation of that response, can be found in appendix B of this report. The attachments will be made available upon request.

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BACKGROUND AND OBJECTIVES

The Housing Authority of the City of San Buenaventura (Authority) was created on September 12, 1949, by the City Council of San Buenaventura. It is a state chartered, federally funded, nonprofit agency with a locally appointed board of commissioners managing and administering housing assistance programs to provide decent, safe, and affordable housing to low- and moderate-income families.

The Authority administers the U.S. Department of Housing and Urban Development (HUD)-funded Low Rent Public Housing and Section 8 Housing Choice Voucher programs. It operates 716 public housing units and manages 1,189 vouchers, with an open waiting list of approximately 2,300 applicants. It was awarded \$719,409 under the Low Rent Public Housing program, \$10,709,814 under the Housing Choice Voucher program, and \$1,252,154 under the Public Housing Capital Fund program for the calendar year 2006.

We received a hotline complaint alleging that the Authority mismanaged and misused federal funds under the Housing Choice Voucher and Low Rent Public Housing programs. Our overall audit objective was to determine whether the Authority's financial activities, operations, and controls complied with HUD requirements.

RESULTS OF AUDIT

Finding 1: The Authority Disregarded Its Payment-in-Lieu-of-Taxes Obligation and Misused HUD Funds

The Authority disregarded its Payment-in-Lieu-of-Taxes obligation, contrary to its consolidated annual contributions contract and cooperation agreement requirements, and used at least \$496,137 in Low Rent Public Housing program funds to purchase nonfederal housing. Authority management was unaware of HUD regulations and agreements restricting the use of Payment-in-Lieu-of-Taxes funds and the use of Low Rent Public Housing program funds. As a result, these funds are no longer available for the operation of the Low Rent Public Housing program or to cover the Authority's obligations to the City of San Buenaventura (City), putting the program at risk.

Payment-in-Lieu-of-Taxes Obligation Requirements Were Ignored

In May 2004 and again in October 2006, the Authority requested a waiver from the City for the Authority's obligation to make annual Payment-in-Lieu-of-Taxes payments pursuant to the terms of its cooperation agreement. The Authority proposed that such funds be used for the increase in supply of low/very low-income housing for the City.

The City did not provide the Authority with a written waiver of its Payment-in-Lieu-of-Taxes obligation. Rather, it notified the Authority that it would recommend that its council deny the Authority's initial request for the waiver. Additionally, based on correspondence between the City and the Authority, the City made it clear that it did not intend to grant the Authority's request. According to the City, withholding the Payment-in-Lieu-of-Taxes payment would be detrimental to its own fiscal operations. Not only would the waiver decrease the amount of funds available to the City, it would also increase its service costs as the Authority would increase the supply of housing, as stated in the Authority's request.

Although the Authority affirmed that it had not received a written waiver, it had withheld payment since fiscal year 2005.

In addition, the Authority had requested HUD's endorsement for the amendment of its cooperation agreement in January 2004, as required in its annual contributions contract. However, even though HUD provided sample formats to be used in obtaining a Board approved waiver for annual Payment-in-Lieu-of-Taxes payments from the City, there is

no indication that HUD formally approved the Authority's request. Furthermore, current Authority management officials stated that they did not believe HUD approval was required. HUD was therefore not informed of the City's lack of approval or the Authority's subsequent actions.

The Payment-in-Lieu-of-Taxes Obligation Was Used to Determine Operating Subsidy

The Authority's Low Rent Public Housing program operating subsidy funding is determined by including a Payment-in-Lieu-of-Taxes expense in its calculation. The Authority reported expenses for Payment-in-Lieu-of-Taxes for fiscal years 2005 and 2006 of \$244,373 and \$245,982, respectively, in its financial submissions to HUD. For its calculation of its Low Rent Public Housing program's operating subsidy for calendar year 2007, the Authority requested additional funding in the amount of \$243,352 for its Payment-in-Lieu-of-Taxes obligation and reported \$233,794 in its financial submission for the fiscal year. HUD provided additional funding to the Low Rent Public Housing program's operating subsidy in all three years for this expense. As a result, the Authority had been receiving funding from HUD for Payment-in-Lieu-of-Taxes obligations it had not met or otherwise spent on the operation of the Low Rent Public Housing program.

Low Rent Funds Were Used for Nonfederal Purposes

In December 2006, the Authority transferred the Payment-in-Lieu-of-Taxes obligated funds for fiscal years 2005 and 2006, totaling \$496,137,¹ to a housing trust fund for the purchase of property that was to be used to develop nonfederal low-income housing units. These funds were then used for the downpayment on a non-HUD property at 1150 North Ventura Avenue. As of the end of our audit period, the Authority had not yet moved the 2007 funds to its housing trust fund, although these funds were also at risk. Management incorrectly considered Low Rent Public Housing program funds set aside for the Payment-in-Lieu-of-Taxes obligation as being available for use for purposes other than the operation of the Low Rent Public Housing program, despite the requirement of the consolidated annual contributions contract and HUD Guidebook 7510.1G restricting the use of the funds. Even if the City had agreed to waive the obligation, Low Rent Public Housing funds must be used for the operation of the Low Rent Public Housing program.

¹ The total low-rent public housing program funds that were transferred exceeded the applicable payment-in-lieu-of-taxes expenses for fiscal years 2005 and 2006 by \$5,782.

Conclusion

The Authority disregarded its Payment-in-Lieu-of-Taxes obligations and requirements for fiscal years 2005 and 2006 and calendar year 2007. Since this obligation is used to determine the Authority's operating subsidy, it is not only essential but required that HUD be notified of any amendments made to the Authority's cooperation agreement. Instead, the Authority transferred Low Rent Public Housing program funds to its housing trust fund and used them for the purchase of property to develop nonfederal low-income housing units. As a result, the Authority received HUD funding for the operation of its Low Rent Public Housing program that it did not expend for the continued operation of that program. Further, the Authority's use of HUD obligated funds on non-HUD program activities put its Low Rent Public Housing program at risk that the necessary funds would not be available when the Payment-in-Lieu-of-Taxes had to be paid.

Recommendations

We recommend that the Director of the Los Angeles Office of Public and Indian Housing require the Authority to

- 1A. Comply with the annual contributions contract and the cooperation agreement with the City by settling its Payment-in-Lieu-of-Taxes obligations to the City.
- 1B. Reimburse the Low Rent Program \$496,137 from nonfederal funds for fiscal years 2005 and 2006 funds paid to the housing trust fund.
- 1C. Cease all transfers of Payment-in-Lieu-of-Taxes obligated funds to the housing trust fund and demonstrate that calendar year 2007 funding in the amount of \$243,353 has not been transferred to the housing trust fund or return the funds to the Low Rent Public Housing program from nonfederal funds.

Finding 2: The Authority Used Low Rent Conventional Housing Funds to Cover Housing Choice Voucher Program Overspending

The Authority overspent its Section 8 Housing Choice Voucher program funding for fiscal year 2007 and used at least \$165,647 of its Low Rent Public Housing program funds to cover the deficit in violation of HUD requirements. The Authority's insufficient accounting controls and lack of written policies and procedures contributed to its cash management problems. Although the Authority restored all borrowed funds, if this practice continues, it may leave the Authority with insufficient resources to operate its programs and place both the Housing Choice Voucher and Low Rent Public Housing programs at risk.

The Authority Overspent Its Available Housing Choice Voucher Program Funding

The Authority overspent its available Housing Choice Voucher program funding and used Low Rent Public Housing program funds to cover operational deficits. During the period October 31, 2006, through May 31, 2007, the Authority experienced deficits in its Housing Choice Voucher program as follows:

Date	Number of units leased	Total housing assistance payments	Total funds available for housing assistance	Overspent housing assistance	Cumulative housing assistance deficit
Oct-06	1,140	\$ 942,429	\$ 924,016	\$ (18,413)	\$ (18,413)
Nov-06	1,151	937,386	914,717	(22,669)	(41,082)
Dec-06	1,164	965,952	902,375	(63,577)	(104,659)
Jan-07	1,164	963,877	904,621	(59,256)	(163,915)
Feb-07	1,172	981,907	903,698	(78,209)	(242,124)
Mar-07	1,173	994,899	907,024	(87,875)	(329,999)
Apr-07	1,170	981,688	903,667	(78,021)	(408,020)
May-07	1,173	981,455	903,890	(77,565)	(485,585)
Totals		\$7,749,593	\$7,264,008	\$ (485,585)	\$ (485,585)

As of September 30, 2006 (end of fiscal year 2006), the Authority maintained Low Rent Public Housing program reserves of \$606,510 and Housing Choice Voucher program reserves of \$319,938 (operating reserves of \$201,316 and administrative reserves of \$118,622). To cover the deficits, the Authority transferred all of its Housing Choice Voucher program reserves (operating and administrative) from its investment account to its general checking account. However, it only had enough reserves to cover its Housing Choice Voucher program deficit through February 2007. Therefore, it overdrew at least \$165,647 to cover the Housing Choice Voucher program payments, and the Authority's

records indicated that only the Low Rent Public Housing program had enough funds to cover these deficits. The Authority's use of Low Rent Public Housing program funds to cover Section 8 expenditures is a violation of the Authority's annual contributions contract and HUD Guidebook 7510.1G requirements.

The Authority received its calendar year 2007 funding in June of 2007, nine months into the fiscal year. The calendar year 2007 funding increase was applied retroactively to January 2007 and created a positive balance in the Section 8 program through its fiscal year ending September 30, 2007. However, it is apparent that the Authority needs to manage its Section 8 program more effectively to avoid funding shortfalls in reliance on HUD funding. Should HUD provide less than expected funding, the Authority would face continuing operating deficits.

The Authority Was Making Financial Management System Control Changes

The Authority's insufficient accounting controls and lack of written policies and procedures contributed to its cash management problems. Its financial management system did not sufficiently identify the changes to its Housing Choice Voucher program reserves and use of Low Rent Public Housing program funds. Since all program funds were maintained in a single checking account, with only its reserves maintained in a separate investment account, the Authority could tap into Low Rent Public Housing funds without showing the cash as having come from that program. In addition, even when cash was moved from the reserve account, the Authority's financial management system failed to properly record the activity. Due to the absence of documented procedures, staff had difficulty in explaining the procedures and controls that were in place between fiscal years 2005 and 2007.

However, the Authority recently began taking corrective actions to repair some of these weaknesses. Specifically, the Authority opened 13 new bank accounts to supersede its current single checking account used to handle all program funds. The new bank accounts are separated by program (Section 8, Low-Rent, Public Housing Capital Fund, etc.) and by asset management project. Additionally, the Authority was restructuring its general ledger system to better track cash, expenses, and revenues. The new system would consist of a master general ledger and subsidiary ledgers for each specific program and each specific asset management project. Lastly, the Authority planned to create written accounting policies and procedures.

Conclusion

The Authority used Low Rent Public Housing program funds to cover its Housing Choice Voucher program overspending for fiscal year 2007. Although the Authority restored all borrowed funds, if this practice continues, it may leave the Authority with insufficient resources to operate its programs and place both the Housing Choice Voucher and Low Rent Public Housing programs at risk. The Authority was working to create written accounting policies and procedures to correct these deficiencies; however, as of the end of our fieldwork, the changes had not been implemented.

Recommendation

We recommend that the Director of the Los Angeles Office of Public and Indian Housing require the Authority to

- 2A. Implement written procedures and controls to ensure that sufficient and appropriate program funds are available before use and to prevent the use of Low Rent Public Housing and Housing Choice Voucher program funds to cover the expenditures of other programs.

SCOPE AND METHODOLOGY

We performed our on-site audit work from September 10 through October 25, 2007, at the Authority located in San Buenaventura, California. The audit generally covered the period October 2004 through September 2007. We expanded our scope when necessary.

To accomplish our objectives, we

- Reviewed applicable HUD regulations under 24 CFR [*Code of Federal Regulations*] Parts 982 and 990, HUD Public and Indian Housing notices, HUD's Program Accounting Handbook 7420.6, and HUD's Low-Rent Technical Guide 7510.1G.
- Obtained an understanding of the Authority's procedures, including its controls to ensure that it properly administered its Section 8 program.
- Reviewed HUD's Los Angeles Office of Public and Indian Housing monitoring reports and files relating to the Authority's financial submissions and interviewed appropriate personnel.
- Reviewed the Authority's independent public accountant reports for fiscal years 2004 through 2006.
- Interviewed Authority Finance Department personnel to acquire an understanding of its financial operations, practices, tracking, and controls.
- Reviewed the Authority's annual contributions contract and cooperation agreement to determine Payment-in-Lieu-of-Taxes obligations and requirements.
- Performed general ledger review for fiscal years 2005 and 2006 to determine whether any Payment-in-Lieu-of-Taxes payments were made to the City and/or county.
- Interviewed City and county personnel to determine whether an agreement was made between the City and county with the Authority relating to the payment of its Payment-in-Lieu-of-Taxes obligation.

We performed our review in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined the following internal controls were relevant to our audit objectives:

- Policies and procedures that management has implemented to ensure accurate, current, and complete disclosure of financial results.
- Policies and procedures that management has implemented to reasonably ensure that its Section 8 program funds are used in accordance with applicable laws and regulations.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

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

- The Authority did not have sufficient controls in place to ensure that its HUD program funds were tracked and spent in accordance with applicable laws and regulations (see findings 1 and 2).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible <u>1/</u>	Funds to be put to better use <u>2/</u>
1B	\$496,137	
1C		\$243,352



- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or federal, state, or local policies or regulations. This includes the total Low Rent Public Housing program funds that were transferred to the housing trust fund. The amount exceeded the applicable fiscal years 2005 and 2006 Payment-in-Lieu-of-Taxes expenses by \$5,782.
- 2/ Recommendations that funds be put to better use are quantifiable savings that are anticipated to occur if an Office of Inspector General (OIG) recommendation is implemented. This includes reductions in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings which are specifically identified. In this instance, if HUD implements our recommendation, \$243,352 in calendar year 2007 Low Rent Public Housing funds, earmarked for the program's Payment-in-Lieu-of-Taxes obligation to the City, will not be transferred to the Authority's housing trust fund and used for nonfederal purposes.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

	<p>HOUSING AUTHORITY of the CITY OF SAN BUENAVENTURA Edward L. Moses, Chief Executive Officer</p>	<p>BOARD OF COMMISSIONERS Kay Doyle, Chair John Polansky, Vice Chair Jill Bangser Fioravanti Sanjuana González Joseph Kreutz Howard Nielsen Bill Watkins</p>
<p>May 5, 2008</p>		
<p>Joan S. Hobbs Regional Inspector General for Audit Office of Inspector General United States Department of Housing and Urban Development Region IX 611 West Sixth Street, Suite 1160 Los Angeles, CA 90017-3101</p>		
<p>Subject: Housing Authority of the City of San Buenaventura Written Response to OIG's Draft Audit Report 2008-LA-10XX</p>		
<p>Dear Ms. Hobbs:</p>		
<p>As per your letter to me dated April 21, 2008, please find enclosed our written response to the findings and recommendations from your recently completed audit of the Housing Authority of the City of San Buenaventura. Also as requested, a Word electronic copy was sent to you on Monday, May 5, 2008.</p>		
<p>Sincerely,</p>		
<p> Edward L. Moses Chief Executive Officer</p>		
<p>cc: K.J. Brockington, Director, Los Angeles Office of PIH Deborah Hernandez, Deputy Assistant Secretary, Office of Field Operations</p>		
<p>ELM:lss</p>		
<p>995 RIVERSIDE STREET VENTURA, CALIFORNIA 93001 [805] 648-5008 • FAX [805] 643-7984</p>		

**HOUSING AUTHORITY
OF THE
CITY OF SAN BUENAVENTURA**

**FINAL
WRITTEN RESPONSE
*TO***

**OFFICE OF INSPECTOR GENERAL
DRAFT AUDIT REPORT 2008-LA-10XX**

**SUBMITTED AT EXIT CONFERENCE
MAY 5, 2008**

HOUSING AUTHORITY OF THE CITY OF SAN BUENAVENTURA

RESPONSE TO FINDING #1: THE AUTHORITY DISREGARDED ITS PAYMENT-IN-LIEU-OF-Taxes Obligations and Misused HUD Funds

Comment 1

The Authority respectfully and strongly disagrees with the above OIG's finding that it disregarded its Payment-in-Lieu-of Taxes obligation to the City of San Buenaventura (City), in accordance with all said agreements governing the matter or that it used \$495,137 of said funds unaware of, without guidance from or in violation of HUD regulations and agreements restricting the use of Payment-in-Lieu-of Taxes funds and the use of Low Rent Public Housing program funds. Further, the Authority concurs that these "defederalized" City funds are no longer available for the operation of the Low Rent Public Housing program because said funds are being used in a manner as directed by and with the full knowledge of the City, to preserve and develop housing for the low and very low income segment of the City's population. Lastly, the Authority respectfully and strongly disagrees with the OIG's finding that the \$496,137 Payment-in-Lieu-of-Taxes funds were not available to cover the cost of the Authority's obligations to the City of San Buenaventura because said "defederalized" City funds were expended, as aforementioned, in a manner as directed by and with full knowledge of the City and in doing so, the Authority *never* put its Low Rent Public Housing program at risk.

Comment 2

CORRESPONDENCE WITH AND GUIDANCE FROM HUD:

Comment 1&3

On January 12, 2004, the Housing Authority sent a letter to Cecelia Ross, Public Housing Director of the Los Angeles HUD field office, asking for support of and guidance on how to accomplish our concept to deposit PILOT funds into a Housing Trust Fund. (Attachment A)

On February 11, 2004, Cecelia Ross, Public Housing Director of the Los Angeles HUD Field Office, responded to our letter (Attachment B), providing a mechanism used in other jurisdictions to accomplish our proposal. In her letter Ms. Ross recommended that a "Waiver In Lieu of Taxes" format "be used in obtaining a Board approved waiver with a resolution in lieu of amending the Cooperation Agreement" and enclosed sample documents to be used to accomplish this process. Then a February 12, 2004 FAX was sent by Ted Skonos of the Los Angeles HUD Field Office, providing a sample document. *Nowhere in Director Ross' letter of Guidance on this matter did she indicate that HUD's approval was necessary or needed to effectuate this process.* Based on this guidance the Authority proceeded with the waiver process.

ESTABLISHING A PILOT AGREEMENT

Comment 4

Housing Authorities are established in the Health and Safety Code of California State Law. Although created in 1949, the Housing Authority of the City of San Buenaventura did not enter into a Cooperation Agreement with the City of San Buenaventura until 1979. Pursuant to this Agreement, all Housing Authority projects are exempt from property taxes and special assessments, and the City will not levy such taxes. The Housing Authority agrees to pay a fee, the PILOT, as a payment for public services and facilities. This fee can be used by the discretion of the City, and has no restrictions on

its use. When the Housing Authority pays this fee, the funds are no longer federal funds with federalized restrictions; it is up to the City how these funds can be spent.

CORRESPONDENCE AND COOPERATION WITH CITY OF SAN BUENAVENTURA:

Comment 5

The Housing Authority exchanged correspondence with the City during 2004 regarding the potential waiver of PILOT funds in order to facilitate the creation of a Housing Trust Fund. During 2004, City management was not interested in formally pursuing our request with City Council.

After changes in City and Authority Executive management, including the employment of a new City Manager and a new Authority CEO, our Agency was approached by the City in September of 2006 to take a lead role in the preservation and development of housing for the low and very low income segment of the population. In that regard, the Housing Authority initiated further discussions with the new City leadership. On October 23, 2006, we formalized our discussions by sending a letter to Rick Cole, City Manager of the City of Ventura; we proposed the deposit of our 2005 and 2006 PILOT funds into a Housing Trust Fund, to be used for housing purposes. Specifically, the PILOT funds were to be used for the acquisition of land and entitlements for property located at 1150 N. Ventura Avenue, the very low-income Soho Apartments (Letter to City already provided). Further, to show their support of the use of these funds for the development of the Soho apartments, City management, during the "further discussions" mentioned above, verbally committed to provide an additional \$1 million of permanent financing in other City funds and instructed the Authority to fill out the appropriate City funding application, detailing the project's permanent financing sources and uses; including PILOT Funds, which would allow City staff to conduct its subsidy layering review, make a recommendation to the City Council and formally receive the City Council's approval of the project's funding and financing methodology.

Comment 6

On October 25, 2006, the Agency's Board of Commissioners passed Resolution 06-16, waiving the payment of funds to the City and placing 2005 and 2006 PILOT funds into a Housing Trust Fund account. The funds were used to pay the down payment for the Soho Apartment development project (final closing statement already provided)

Comment 5

As previously mentioned, the City was fully aware of this use of PILOT funds for the Soho Apartment project. Several discussions were held with City staff regarding the source of acquisition funding. In our funding application to the City dated June 15, 2007 we specifically called out the use of the PILOT funds in our Sources and Uses project financing details (Attachment C). This application was favorably considered by the City Council on March 10, 2008, when the City Council approved a residual receipt loan of \$1 million to the Soho Project (Attachment D).

Comment 7

On March 27, 2008, we sent a follow-up letter to Rick Cole addressing 2007 PILOT funds and all future PILOT funds. We ask for City Council consideration of this request. (Attachment E)

In an April 14, 2008 meeting with the City's Community Development Director, specifically called in response to the Agency's March 27th letter (referenced above)

Comment 7

and pursuant to the City Manager's instruction, the Community Development Director verbalized City management support of the PILOT waiver proposal (Nelson Hernandez e-mail dated April 21, 2008; Attachment F) and instructed the Agency to work with the City Clerk to schedule a Resolution for City Council action in early summer 2008. The Authority has initiated this process.

Comment 5

As evidenced by the aforementioned City Council approval, we are working cooperatively with the City to further our mutual goals of development of housing for very low income residents of our community. We obtained City Council endorsement of the use of 2005 and 2006 PILOT funds for the Soho Project and will soon formalize approval of 2007 and all future PILOT funds for Housing Trust Fund purposes.

Comment 4

In conclusion, these funds become defederalized upon computation as fees owed the City per the Cooperation Agreement. This money loses its federal designation and becomes City funds used at the discretion of the City Council and City administration.

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Comment 8

Finding 2: The Authority Used Low Rent Funds to Cover Housing Choice Voucher Program Overspending.

Authority's Response -

The Housing Authority was managing all programs from a single checking account. This financial system was impractical and inefficient.

The Board of Commissioners of the Housing Authority by resolution (resolution No. 07-06 **Attachment #1**) approved and authorized the opening of separate checking accounts for the efficient and better accountability of the Authority's subsidized programs.

Also, the Chief Financial Officer added two monthly reports:

The Section 8 Housing Assistance Payment Analysis to monitor the total funds available for Housing Assistance payments.

The Section 8 Administrative Analysis to monitor the program expenditures.

These two reports will ensure that appropriate and timely adjustments are made to the Housing Choice Voucher Program to maintain a viable program at its highest possible level. The goal of the Housing Authority is to assist as many needy families as possible within the limits of the program.

The above accounting controls and procedures were in place and disclosed to the staff of the Office the Inspector General during their review of the Authority's financial records. Also attached is a draft monitoring procedure (**Attachment #2**) which we will wait for your guidance on implementation.

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OIG Evaluation of Auditee Comments

Comment 1 Our finding that the Authority disregarded its Payment-in-Lieu-of-Taxes obligation, contrary to all said agreements governing the use of \$495,137 of Payment-in-Lieu-of-Taxes funds, without guidance from or in violation of HUD regulations is based on: (1) the Cooperation Agreement between the Authority and the City of Ventura that requires the Authority to make Payments-in-Lieu-of-Taxes at the end of each fiscal year to the City. The agreement also stipulates that it "shall not be abrogated, changed, or modified without the consent of the Government [HUD]." Additionally, (2) the Annual Contributions Contract between HUD and the Authority requires the Authority to "perform and comply with all applicable provisions of the Cooperation Agreement(s)," including meeting their Payments-in-Lieu-of-Taxes obligation to the City, and "shall not terminate or amend the Cooperation Agreement(s) without the written approval of HUD." Although neither the City nor HUD approved a waiver or change to the agreements, the Authority did not pay its Payments-in-Lieu-of-Taxes obligation to the City for fiscal years 2005 and 2006.

The Annual Contributions Contract also restricts the use of all funds controlled under this agreement, including Low Rent Public Housing program funds, and requires that the Authority may only use such funds for "(1) the payment for expenses related to the development and operation of projects; (2) the purchase of investment securities as approved by HUD; and (3) other purposes specifically approved by HUD." The Authority withdrew \$496,137 from its Payments-in-Lieu-of-Taxes accrual account and transferred the funds into a Housing Trust Fund and used \$495,725 as a down payment for property to develop low-income nonfederal funded housing units. The Authority's use of these Annual Contributions Contract controlled funds was therefore in violation with the Annual Contributions Contract.

Although the Authority sought HUD's guidance in January 2004, proposing to amend its Cooperation Agreement with the City of Ventura, HUD did not formally approve the use of Payments-in-Lieu-of-Taxes funds for any specific purpose. HUD simply provided sample formats in which to obtain a waiver from the City, which the Authority did not obtain. Furthermore, the examples provided were to defray the operating expenses of the subject Authority, not for use in developing nonfederal property.

As a result, the Authority is still liable to the City for Payments-in-Lieu-of-Taxes under the Cooperation Agreement, and until it disburses the funds allocated for Payments-in-Lieu-of-Taxes to the City, they remain operating subsidy funds subject to the Annual Contributions Contract.

Comment 2 The funds in question were funded to the Authority for the purpose of paying the Authority's Payments-in-Lieu-of-Taxes obligation to the City. Therefore, the

funds are subject to the Authority's Annual Contributions Contract and Cooperation Agreements and are considered federal funds until they are used "(1) for expenses related to the development and operation of projects; (2) the purchase of investment securities as approved by HUD; and (3) other purposes specifically approved by HUD."

Moreover, the Authority has not provided documentation indicating that the Payments-in-Lieu-of-Taxes funds were being used as directed by the City. The Authority did provide an application for funding to the City with a letter of intent stating that the Authority's Board of Commissioners passed a resolution placing their 2004 and 2005 Payments-in-Lieu-of-Taxes funds into a Housing Trust Fund. The funds would be used for the downpayment, loan fees, and interest to acquire the property noted on the application. However, the City did not provide a written approval or waiver for the use of the Payments-in-Lieu-of-Taxes funds. Additionally, our contact with the City indicates that it has no intention of waiving the Authority's Payments-in-Lieu-of-Taxes obligation. Until the City Council officially waives the obligation in conjunction with HUD's approval and/or it specifically approves the current use as fulfilling the obligation, the Payments-in-Lieu-of-Taxes are still owed to the City.

Also, because the Authority has already expended the funds provided by HUD for the Authority's Payments-in-Lieu-of-Taxes obligation, these funds are no longer available for use for the operation of the Low Rent Public Housing program.

- Comment 3** Although we agree that in Director Ross' letter of guidance she did not indicate that HUD's approval was necessary, the Authority is subject to its Annual Contributions Contract and Cooperation Agreements. Additionally, HUD provided guidance on how to achieve a written waiver of Payments-in-Lieu-of-Taxes from the City; however, the Authority has yet to attain one. The Authority did not inform HUD that it withheld payment despite the lack of City approval.
- Comment 4** We agree that the Payments-in-Lieu-of-Taxes fee can be used at the discretion of the City. We are also aware that once the Authority pays the Payments-in-Lieu-of-Taxes to the City the funds are no longer subject to HUD regulations and the City may choose how to spend these funds. Nevertheless, the Payments-in-Lieu-of-Taxes were not paid to the City for fiscal years 2005 and 2006, as required by both the Annual Contributions Contract and Cooperation agreements, and therefore are still subject to the Annual Contributions Contract and were not expended for the intended obligation.
- Comment 5** We agree that the Authority did propose to the City that the deposit of the 2005 and 2006 Payments-in-Lieu-of-Taxes funds be placed into a Housing Trust fund. However, even though some City officials may have been fully aware of the Authority's use of Payments-in-Lieu-of-Taxes funds for the SOHO project, the City has not officially waived nor approved the use of these funds.

In addition, the Authority has not provided documentation indicating that the Payments-in-Lieu-of-Taxes funds were being used as directed by the City. The Authority did provide an application for funding to the City with a letter of intent stating that the Authority's Board of Commissioners passed a resolution placing their 2004 and 2005 Payments-in-Lieu-of-Taxes funds into a Housing Trust Fund. Accordingly, the funds would be used for the downpayment, loan fees, and interest to acquire the property noted on the application. Nonetheless, the City did not provide an explicit written approval nor waiver for the use of the Payments-in-Lieu-of-Taxes funds. Additionally, we did not find any reference of the use of Payments-in-Lieu-of-Taxes funds as "Sources and Uses" in the project financing details contained in both the City Council's approved meeting minutes and the Administrative Report presented to the City Council in March 2008 requesting approval on the SOHO project loan. As a result, it is not clear if the City Council has been made fully aware of the Authority's actions, which took place over a year before this meeting, or the impact on the City's fiscal operations. Furthermore, our contact with the City indicates that it has no intention of waiving the Authority's Payments-in-Lieu-of-Taxes obligation. Therefore, the Authority expended the obligated Payments-in-Lieu-of-Taxes funds before obtaining the required written approval from the City Council on the use and purpose of such funds.

Comment 6 We agree the Authority's Board of Commissioners passed a resolution waiving the payment of funds to the City and placing the 2004 and 2005 Payments-in-Lieu-of-Taxes into a Trust Fund, not including 2006 accrued Payments-in-Lieu-of-Tax funds; however, the Authority failed to obtain a resolution from the City's Board of Commissioners as recommended by HUD in its February 2004 response. The Cooperation Agreement is between the City and the Authority, therefore an agreement must be made between both parties for any proposed amendments. As a result, the Authority's Board of Commissioners may not solely make any amendments to the Cooperation Agreement.

Comment 7 To date there has been no official approval of the Authority's Payments-in-Lieu-of-Taxes waiver proposal from the City, which should have been obtained before the funds were withheld and disbursed for the SOHO project. In addition, the Authority has made numerous attempts to attain the City's approval; however, the City has not provided one. Therefore, the Authority has disregarded its Payments-in-Lieu-of-Taxes obligation and misused HUD funds.

Comment 8 As mentioned in the audit report, we agree with the Authority that measures are being taken to ensure that Low Rent Public Housing program funds are not used to cover Section 8 deficits. We found that the use of separate bank accounts, monthly programmatic monitoring reports, and written policies and procedures will enhance the control environment.

The written procedures provided by the Authority are a step in the right direction. However, our recommendation remains unchanged so that HUD can take the

necessary steps to review implementation of the additional controls enacted by the Authority. In addition, we believe the procedures presented by the Authority are not complete. The new policies and procedures should include details on new accounting procedures enacted, ability to track program funds within the accounting system, monitoring of program bank accounts and monthly reconciliations of program funds. Additionally, the new policies and procedures should include references to HUD rules and regulations and the Authority's Administrative Plan where applicable.

Appendix C

CRITERIA

The Consolidated Annual Contributions Contract, Number SF-194, March 22, 2002, states as follows:

- **Section 6, Cooperation Agreement(s)**, states that the Authority must perform and comply with all applicable provisions of the cooperation agreement(s) including the making of payments in lieu of taxes. The Authority may not terminate or amend the cooperation agreement(s) without the written approval of HUD.
- **Section 9(C)(1), Depository Agreement and General Fund**, states that the Authority may only use funds outlined under the annual contributions contract for payment of expenses related to the development and operation of projects controlled under the provisions of the annual contributions contract.

The Cooperation Agreement between the City of San Buenaventura and the Authority, section 9, requires the Authority to pay an annual Payment-in-Lieu-of-Taxes to the City at the end of each fiscal year in the amount of 10 percent of the shelter rent received from its tenants or the amount permitted by applicable state law, whichever amount is lower. Additionally, it states that the agreement cannot be modified without the consent HUD.

24 CFR [Code of Federal Regulations] 982.152(a)(3) states, “HA [housing authority] administrative fees may only be used to cover costs incurred to perform HA administrative responsibilities for the program in accordance with HUD regulations and requirements.”

24 CFR 982.153, PHA [Public Housing Authority] Responsibilities, requires public housing authorities to “comply with the consolidated ACC [annual contributions contract], the application, HUD regulations and other requirements, and the PHA administrative plan.”

24 CFR 982.155(a), Administrative Fee Reserve, states, “the PHA [public housing authority] must credit to the administrative fee reserve the total of (1) the amount by which program administrative fees paid by HUD for a PHA fiscal year exceeded the PHA program administrative expenses for the fiscal year; plus (2) Interest earned in the administrative fee reserve.”

24 CFR 982.156, Depository [sic] for Program Funds, states that a “PHA [public housing authority] may only withdraw deposited program receipts for use in connection with the program in accordance with HUD requirements.”

24 CFR 982.158(a), Program Accounts and Records, requires public housing authorities to maintain complete and accurate accounts and other records for the program in accordance with HUD requirements. Additionally, they must provide HUD with accounts and other records, reports, documents, and information as requested.

24 CFR 990.190(c), Other Formula Expenses (add-ons), states that in addition to calculating a public housing authority's operating subsidy based on the project and utilities expense level, an authority's eligible formula expenses, used to calculate its operating subsidy, may be increased by allowed add-on expenses. An amount for payment in lieu of taxes in accordance with section 6(d) of the United States Housing Act of 1937 may be added as an eligible expense in determining the authority's annual operating subsidy.

PIH [Public and Indian Housing] Low-Rent Technical Accounting Guide 7510.1G, chapter 2-13, requires housing authorities to establish sufficient controls to ensure proper accounting for cash and full identification of audit trails. "Accounting controls ensure that the accounting system used by the HA [housing authority] accurately identifies the source, use, and remaining balance of individual program cash resources." Additionally, all funds received from HUD program funding are "restricted to the specific purposes authorized in the program budgets." Chapter 2-15, stipulates that even though funds may be pooled together for any expenditures chargeable to the housing authority's programs, program funds are not fungible and "funds shall not be withdrawn for a program in excess of the amount of funds on deposit for that particular program." All funds pooled together that result in "due to/due from" transactions must be "reconciled at the end of each reporting period to ensure that they are in balance." Further, chapter 11-16 specifies that all funds provided by HUD are to be used by the housing authority only for the purposes for which the funds are authorized.

PIH Notice 2005-09, Public Housing Agency (PHA) Flexibility to Manage the Housing Choice Voucher Program in 2005, states that "starting in calendar year 2005, the Department will no longer exercise its option to establish and maintain an Annual Contributions Contract (ACC) reserve account for the voucher program."

PIH Notice 2006-03, Reduction of Annual Contributions Contract (ACC) Reserves, Recession of Requirements under Form HUD-52681 for Most Housing Choice Voucher Program Units, and Sanctions for Failure to Submit Required Financial Reports Pursuant to 24 CFR 5.801, reduces any unused annual contributions contract reserves remaining after December 31, 2005, to zero. It also outlines the accounting requirements for any budget authority and administrative fees provided to housing authorities for calendar year 2005. Specifically, beginning January 1, 2005, excess budget authority funds received by public housing authorities that are not used to pay housing assistance payments will become part of the undesignated fund balance account. Such funds may only be used to assist additional families up to the number of units under contract. Administrative fees received in excess of administrative expenses will also become part of the undesignated fund balance account. These funds will remain as administrative fee reserves and are subject to all requirements applicable including 24 CFR 982.155. Moreover, "a PHA [public housing authority] must be able to differentiate HAP [housing assistance payment] equity (budget authority in excess of HAP expenses) from Administrative Fee equity (Administrative Fees earned in excess of administrative costs.)"

PIH Notice 2005-01, Implementation of the Consolidated Appropriations Act (HR 4818-H Rept 108-792), 2005 Funding Provisions for the Housing Choice Voucher Program, stipulates that administrative fees provided from this appropriation shall only be used for activities related to the provisions of Section 8 tenant-based rental assistance, including related

development activities. Also, it prohibits the use of renewal funds for overleasing. “PHAs [public housing authority] must manage their programs in a prudent manner, to enable them to serve families within their calendar year 2005 budget and voucher baseline. PHAs should review their policies and operations, to ensure they are not incurring HAP [housing assistance payment] costs beyond what is needed to support decent housing of a modest nature within market rents for participants.” Administrative fees received from fiscal year 2006 funding that are later moved into an undesignated fund account are subject to 24 CFR 982.155.

PIH Notice 2006-05, Implementation of the 2006 HUD Appropriations Act (Public Law 109-115), Funding Provisions for the Housing Choice Voucher Program, continues to prohibit the use of renewal funds for overleasing. “Additionally, this Notice provides that any budget authority provided to PHAs [public housing authority] in CY [calendar year] 2006 that exceeds actual program expenses for the same period must be maintained in the PHA’s undesignated fund balance account in accordance with Generally Accepted Accounting Principles (GAAP).” Moreover, administrative fees received from federal fiscal year 2006 funding that are later moved into an undesignated fund account are subject to 24 CFR 982.155.

PIH Notice PIH 2007-14, Implementation of Federal Fiscal Year 2007 Funding Provisions for the Housing Choice Voucher Program, Restrictions on Housing Assistance Payment Equity (HAP) Accounts, states, “Public housing authorities are reminded that funds in the Net Cumulative HAP Equity account (formerly known as Undesignated Fund Balance – HAP) generated from calendar year 2005 and later appropriations may only be used for HAP needs in that year and future calendar year HAP needs of the Housing Choice Voucher program, keeping in mind current and any future restrictions on over-leasing. Calendar year funds may not be used to cover any prior year deficits. However, public housing authorities may use funds in the Administrative Fee Equity account for such purposes.”