



City of Hawthorne, CA

HOME Investment Partnerships Program



Issue Date: September 13, 2013

Audit Report Number: 2013-LA-1009

TO: William Vasquez, Director, Los Angeles Office of Community Planning and Development, 9DD

Tanya E. Schulze

FROM: Tanya E. Schulze, Regional Inspector General for Audit, Los Angeles Region, 9DGA

SUBJECT: The City of Hawthorne Inappropriately Used Nearly \$1.6 Million in HOME Funds for Section 8 Tenants

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our review of the City of Hawthorne's HOME Investment Partnerships Program.

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 8L, requires that OIG post its publicly available reports on the OIG Web site. 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.



September 13, 2013

The City of Hawthorne Inappropriately Used Nearly \$1.6 Million in HOME Funds for Section 8 Tenants

Highlights

Audit Report 2013-LA-1009

What We Audited and Why

We audited the City of Hawthorne because of a corrective action verification audit done by the Office of Inspector General (OIG) that identified \$840,741 in HOME Investment Partnerships Program funds that were transferred to the Section 8 program between 2005 and 2006 (2013-LA-0802). The objectives of the audit were to determine (1) the eligibility of \$840,741 in 2005 and 2006 HOME program transfers to the Section 8 program, (2) whether the funds were repaid to the HOME program, (3) what activities the City informed the U.S. Department of Housing and Urban Development's (HUD) Office of Community Planning and Development would be performed with the funds, and (4) how HOME funds were used in later years.

What We Recommend

We recommend that the Director of HUD's Los Angeles Office of Community Planning and Development require the City to (1) repay the HOME program account nearly \$1.6 million for ineligible HOME funds that were used for Section 8 housing assistance payments and (2) develop and implement written policies and procedures for the HOME program.

What We Found

The City used nearly \$1.6 million of its 2004 and 2005 HOME funds for ineligible activities, which were not repaid to the HOME program. Although the City informed HUD's Office of Community Planning and Development that it would use the funds for various items, including a HOME tenant-based rental program, it used its HOME funds to cover shortfalls in Section 8 rental assistance payments.

Although no HOME funds were used for the Section 8 program in later years, the City had not developed written policies and procedures for its HOME program.

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BACKGROUND AND OBJECTIVES

The HOME Investment Partnerships Program is authorized under Title II of the Cranston-Gonzalez National Affordable Housing Act. The program regulations are contained in 24 CFR (Code of Federal Regulations) Part 92 and the HOME Investment Partnerships Program Final Rule. HOME funds are awarded annually as formula grants to participating jurisdictions and used to fund a wide range of activities that build, buy, or rehabilitate affordable housing for rent or home ownership or provide direct assistance to low-income households. The program allows State and local governments to use HOME funds for grants, direct loans, loan guarantees or other forms of credit enhancement, rental assistance, or security deposits. The manner in which the grantee expects to expend its HOME funds is detailed in its consolidated plan. The consolidated plan is carried out through annual action plans, which provide a concise summary of the actions, activities, and specific Federal and non-Federal resources that will be used each year to address the priority needs and specific goals identified by the consolidated plan.

The City of Hawthorne is located at 4455 West 126th Street, Hawthorne, CA. Incorporated in 1922, the City has a population of nearly 87,000 within a 6-square-mile area. There are several departments that help run the City. The Community Development department is responsible for administering the federally funded Community Development Block Grant and HOME program. Community Development activities include housing rehabilitation, mortgage assistance, economic development assistance, commercial rehabilitation, public improvements, code enforcement, and various public services.

The City used its HOME funding for program years 2004 through 2011 for the Housing Rights Center; the security deposit assistance, single-family and multifamily rehabilitation, and tenant-based rental assistance programs; and the general administration of these programs. According to the City, its tenant-based rental assistance program was designed “to leverage HUD [U.S. Department of Housing and Urban Development] Section 8 voucher funds, the City will provide tenant based rental assistance to extremely low and low income households. Similar to the [City’s] Section 8 Voucher Program, this program will provide rental payments to landlords on behalf of extremely low and low income tenants.”

The Office of Inspector General (OIG) conducted a corrective action verification (memorandum report 2013-LA-0802, issued February 15, 2013) of the Office of Public Housing’s closure of an audit recommendation related to the City’s public housing funds. As part of that review, OIG found that the City transferred \$840,741 in HOME funds to its Section 8 Housing Choice Voucher program. It concluded that a follow-up review of the City’s HOME program was warranted given the City’s potentially questionable use of funds.

Our objectives were to determine (1) the eligibility of \$840,741 in 2005 and 2006 HOME program transfers to the Section 8 program, (2) whether the funds were repaid to the HOME program, (3) what activities the City informed HUD’s Office of Community Planning and Development would be performed with the funds, (4) and how HOME funds were used in later years.

RESULTS OF AUDIT

Finding: The City of Hawthorne Inappropriately Used Nearly \$1.6 Million in HOME Funds for Section 8 Tenants

The City inappropriately used nearly \$1.6 million of its HOME funds for program years 2004 and 2005 to cover Section 8 rental assistance payments. This condition occurred because the City did not properly consider all of the relevant HUD criteria and had no written policies and procedures for its HOME program. As a result, the funding was not available to be used on the intended persons through eligible HOME activities.

The City Used HOME Funds for Ineligible Activity

The City inappropriately used nearly \$1.6 million in HOME funds for its Section 8 Housing Choice Voucher program,¹ including

- \$768,541 used for housing assistance payments in program year 2004,
- \$754,372 used for housing assistance payments in 2005, and
- \$72,200 used for associated administrative fees in 2005.²

Our review of the applicable tenants' files or forms HUD-50058³ showed that all of the tenants were Section 8 program participants. Although criteria at 24 CFR 92.205(a) and 92.209(k) allow HOME funds to be used for tenant-based rental assistance, additional criteria at 2 CFR Part 225 (Office of Management and Budget Circular A-87) does not allow cost allocable to a Federal award to be charged to other Federal awards to overcome fund deficiencies or for other reasons (see Appendix C). Therefore, since the City used the HOME funds to pay for Section 8 funding shortfalls, making the housing assistance payments and paying associated administrative fees for Section 8 tenants was an ineligible use of HOME funds. The City confirmed that the funds were not later returned to the HOME program.

¹ The Section 8 Housing Choice Voucher program is a federally funded program provided through HUD's Office of Public Housing. This program provides decent, safe, and sanitary housing rental assistance for very low-income families, the elderly, disabled families, and other individuals by making housing assistance payments on behalf of the tenant to the landlord. The City's housing authority administers the program locally.

² The \$768,541 and \$72,200, totaling \$840,741, were identified in audit memorandum 2013-LA-0802, issued February 15, 2013 (see Background and Objective).

³ Form HUD-50058 is a document used to collect, store, and generate reports on families that participate in public housing or Section 8 rental subsidy programs.

The City Did Not Adequately Inform HUD

During the 2004 program year, the City amended its final consolidated plan and annual action plan to reallocate \$768,541 in HOME funding. The City's former director of planning and community development informed the city council that the reallocation was necessary to cover a shortfall in Section 8 rental assistance payments. However, the letter informing HUD's Office of Community Planning and Development of the amendment did not mention that this funding was being reallocated to cover Section 8 program shortfalls. The City stated that it created a tenant-based rental assistance program in accordance with 24 CFR 92.205(a) and 92.209(k) requirements.

The City's 2005-2009 final consolidated plan from May 2005, provided to HUD's Office of Community Planning and Development, included contradictory information on how the HOME funds would be used for 2005-2006. It stated that HOME funds would be used for a tenant-based rental assistance program that was identified as being "Similar to the Section 8 Voucher Program." However, another section stated that it would "provide tenant based assistance to 50 extremely low and low income Section 8 tenants as needed."

The City provided information to HUD's Office of Public Housing through its Section 8 Voucher Management System submissions, which clearly stated that housing assistance payments were being funded by HOME funds due to a lack of availability of HUD funds.⁴ However, the City did not provide this information to HUD's Office of Community Planning and Development, which monitors the HOME funding.

The City Did Not Consider All Relevant Criteria

HOME criteria at 24 CFR 92.205(a) and 92.209(k) allow a tenant-based rental assistance program similar to the Section 8 program and allow HOME tenants to qualify for and transfer to the Section 8 program later. As a result, the City did not realize it was improper and thought it could fund preexisting Section 8 tenants with HOME funds. However, it did not consider 2 CFR Part 225. Also, the City had no written policies and procedures for its HOME program, including the selection of eligible tenants for a tenant-based rental assistance program.

⁴ As discussed in memorandum report 2013-LA-0802, the HUD Office of Public Housing later identified this matter and notified the Office of Community Planning and Development and then OIG.

The City Stopped Using HOME Funds for Section 8 in Later Years

Although the City did not use HOME funds for its tenant-based rental assistance program in program years 2006 and 2007, it did use HOME funds for its tenant-based rental assistance program in program years 2008 through 2011. Our review of the files for tenants assisted by the HOME program for those years showed that they were not Section 8 participants but actual HOME program participants. City staff stated that the former director of planning and community development had initially instructed staff to use Section 8 tenants for the HOME program but later instructed staff to start pulling applicants from the City's Section 8 waiting list or other sources to generate participants for its HOME tenant-based rental assistance program, with the intent of helping to further the City's overall rental assistance to low-income persons. While the City had begun operating its HOME tenant-based rental assistance program properly in respect to the use of Section 8 tenants, it had not developed written policies and procedures for its HOME program to avoid future problems, which was a control weakness.

Conclusion

The City inappropriately used nearly \$1.6 million in HOME funds for Section 8 tenants in program years 2004 and 2005 and did not adequately inform HUD about its intended use for the funds. This condition occurred because the City did not consider all of the applicable criteria and did not realize it was improper. As a result, the funding was not available to be used for the intended persons through eligible HOME activities. Although the City operated its tenant-based assistance program appropriately in later years, it should develop written policies and procedures for its HOME program to strengthen its controls.

Recommendations

We recommend that the Director of HUD's Los Angeles Office of Community Planning and Development require the City to

- 1A. Reimburse its HOME program \$1,595,113 from non-Federal funds for HOME funds that were inappropriately used on Section 8 housing assistance payments.
- 1B. Develop and implement written policies and procedures for its HOME program.

SCOPE AND METHODOLOGY

We performed our onsite work at the City of Hawthorne's City Hall located at 4455 West 126th Street, Hawthorne, CA, between January 29 and July 11, 2013. The audit scope covered the period July 1, 2004, through June 30, 2011, and was extended as necessary.

To accomplish our objectives, we

- Reviewed relevant HOME program regulations.
- Reviewed the City's consolidated plan and action plan for program year 2004.
- Reviewed consolidated annual performance and evaluation reports for program years 2005 through 2011.
- Reviewed the City's expenditure detail reports for program years 2005 through 2011.
- Reviewed tenant files and forms HUD-50058.
- Obtained and reviewed pertinent information from HUD's Public and Indian Housing Information Center.
- Reviewed program expenditures.
- Interviewed applicable HUD and City representatives.

We reviewed the entire population of tenant files for participants listed as being part of the HOME tenant-based rental assistance program for program years 2004 (62 tenants) and 2005 (68 tenants). These numbers represent the total amount of individuals who received rental assistance from the HOME tenant-based rental assistance program. We reviewed each file to determine whether the participant was a HOME program tenant or a Section 8 tenant. In the event that the tenant file was unavailable, we reviewed the tenant's form HUD-50058 to make that determination. We verified computer-generated data from the auditee by selecting a sample of tenants from the Tenants Under HOMEFUNDS list and then verifying the amounts paid to the landlord via the Vendor Master Report, which comes from the City's accounting software. We selected a non-statistical sample of 7 tenants out of the populations of 68. We then reviewed the same 3 months for each tenant (July 2005, January 2006, and June 2006), which were all selected randomly.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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 objectives:

- Controls over compliance with Federal laws and regulations.
- Controls over the City's policies and procedures.

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 Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The City did not comply with Federal regulations regarding not allowing a Federal award to be charged to other Federal awards to overcome fund deficiencies or for other reasons (finding).
- The City lacked any policies or procedures to ensure that the tenants served under the HOME tenant-based rental assistance program were eligible participants (finding).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Ineligible 1/
1A	\$1,595,113

- 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.

Appendix B

AUDITEE COMMENTS

We provided the City an opportunity to respond to this report in writing, which would be included as an appendix to the report, with a submission due date of August 27, 2013. Per the auditee's request, we extended that date to August 30, 2013. The City notified us on September 3, 2013 that it was not submitting written comments.

Appendix C

CRITERIA

2 CFR Part 225 (Office of Management and Budget Circular A-87)
Appendix A to Part 225 - General Principals for Determining Allowable Costs

C. Basic Guidelines

3. Allocable costs.

c. Any cost allocable to a particular Federal award or cost objective under the principles provided for in 2 CFR part 225 may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by law or terms of the Federal awards, or for other reasons.

§ 92.205 Eligible Activities: General

a. Eligible activities.

1. HOME funds may be used by a participating jurisdiction to provide incentives to develop and support affordable rental housing and homeownership affordability through the acquisition (including assistance to homebuyers), new construction, reconstruction, or rehabilitation of non-luxury housing with suitable amenities, including real property acquisition, site improvements, conversion, demolition, and other expenses, including financing costs, relocation expenses of any displaced persons, families, businesses, or organizations; to provide tenant-based rental assistance, including security deposits; to provide payment of reasonable administrative and planning costs; and to provide for the payment of operating expenses of community housing development organizations. The housing must be permanent or transitional housing. The specific eligible costs for these activities are set forth in §§ 92.206 through 92.209.
2. Acquisition of vacant land or demolition must be undertaken only with respect to a particular housing project intended to provide affordable housing.
3. Conversion of an existing structure to affordable housing is rehabilitation, unless the conversion entails adding one or more units beyond the existing walls, in which case, the project is new construction for purposes of this part.
4. Manufactured housing. HOME funds may be used to purchase and/or rehabilitate a manufactured housing unit, or purchase the land upon which a manufactured housing unit is located. Except for existing, owner-occupied manufactured housing that is rehabilitated with HOME funds, the manufactured housing unit must, at the time of project completion, be connected to permanent utility hook-ups and be located on land that is owned by the manufactured housing unit owner or land for which the manufactured housing owner has a lease for a period at least equal to the applicable period of affordability.

§ 92.209 Tenant-based Rental Assistance: Eligible Costs and Requirements

k. *Program operation.* A tenant-based rental assistance program must be operated consistent with the requirements of this section. The participating jurisdiction may operate the program itself, or may contract with a PHA [public housing agency] or other entity with the capacity to operate a rental assistance program. The tenant-based rental assistance may be provided through an assistance contract to an owner that leases a unit to an assisted family or directly to the family. In either case, the participating jurisdiction (or entity operating the program) must approve the lease.

1. *Use of Section 8 assistance.* In any case where assistance under section 8 of the 1937 Act becomes available to a participating jurisdiction, recipients of tenant-based rental assistance under this part will qualify for tenant selection preferences to the same extent as when they received the tenant-based rental assistance under this part.