



Municipality of Carolina, PR

HOME Investment Partnerships Program



Issue Date: August 8, 2014

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TO: María Ortíz, Director, Community Planning and Development, San Juan Field Office, 4ND

//signed//

FROM: Nikita N. Irons, Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: The Municipality of Carolina Did Not Properly Administer Its HOME Program

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our review of the Municipality of Carolina'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 8M, 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 404-331-3369.



August 8, 2014

The Municipality of Carolina Did Not Properly Administer Its HOME Program

Highlights

Audit Report 2014-AT-1007

What We Audited and Why

We audited the Municipality of Carolina's HOME Investment Partnerships Program as part of our strategic plan, based on the amount of HOME funds approved. The objectives of the audit were to determine whether HOME-funded activities met program objectives, home buyers complied with HOME's primary residency requirement for the duration of the period of affordability, and the Municipality maintained a financial management system in compliance with the U.S. Department of Housing and Urban Development's (HUD) requirements and reported accurate and supported information in HUD's Integrated Disbursement and Information System.

What We Recommend

We recommend that HUD (1) determine the eligibility of more than \$8.6 million in unsupported HOME program costs and activities that showed signs of slow progress, (2) deobligate and put to better use more than \$387,000 in overstated obligations, (3) require the repayment of more than \$62,204 in ineligible expenditures, and (4) remit to its treasury account \$56,102 in unexpended funds.

What We Found

The Municipality disbursed HOME funds for three activities that showed signs of slow progress without assurance that the activities would generate the intended benefits. In addition, it did not ensure that the principal residency requirement was met for the duration of the period of affordability for 35 home buyers. As a result, HUD had no assurance that more than \$8.2 million disbursed for HOME-funded activities met program objectives and fully provided the intended benefits.

The Municipality's financial management system did not properly identify the source and application of more than \$726,000 in HOME funds and did not support the eligibility of more than \$68,000 in program disbursements. In addition, the Municipality allowed the use of more than \$62,000 for ineligible expenditures, did not remit to its treasury account more than \$56,000 in unexpended drawdowns, and consistently maintained a high cash balance in its bank account. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for authorized purposes and in accordance with HUD requirements.

The Municipality did not ensure the accuracy of commitments and other information entered into HUD's information system. It did not support more than \$387,000 in HOME commitments and failed to report more than \$233,000 in program income receipts in HUD's information system. As a result, HUD had no assurance that the Municipality met HOME program commitment and disbursement requirements.

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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 as amended. The U.S. Department of Housing and Urban Development (HUD) allocates funds by formula to eligible State and local governments for the purpose of increasing the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families. State and local governments that become participating jurisdictions may use HOME funds to carry out multiyear housing strategies through acquisition, rehabilitation, new housing construction, and tenant-based rental assistance.

Participating jurisdictions are required to commit HOME funds within 24 months and expend them within 5 years after the last day of the month in which HUD notifies the participating jurisdiction of HUD's execution of the HOME agreement.¹ In addition to the HOME program's regulatory 5-year disbursement requirement, the National Defense Authorization Act of 1991 (Public Law 101-510, dated November 5, 1990) requires that on September 30 of the fifth year after the period of availability for obligation of a fixed-appropriation account ends, the account be canceled and, thereafter, not be available for obligation or expenditure for any purpose.² Participating jurisdictions are required to expend, for eligible costs, HOME funds drawn down from the treasury account within 15 days. Any unexpended drawdowns must be returned to the treasury account. HUD also requires that HOME funds in the participating jurisdiction's local bank account, including program income and recaptured funds,³ be disbursed before additional grant funds are requested.

Participating jurisdictions draw down HOME funds through HUD's Integrated Disbursement and Information System. HUD's information system is also used to monitor and track HOME commitments, program income, repayments, and recaptured funds, among other things. In addition, HUD uses the data that the participating jurisdiction provides in HUD's information system to report on the performance of the HOME program to Congress and other program stakeholders.

The Municipality of Carolina was founded in 1857. The governing system consists of an executive and legislative body elected for 4-year terms. The Municipality is the fifth largest local participating jurisdiction in Puerto Rico, for which HUD has approved more than \$14.7 million in HOME funds during the last 11 fiscal years. HUD's information system reflected HOME drawdowns exceeding \$19 million between January 2001 and October 2013.

¹ For purposes of determining compliance with commitment and disbursement requirements, HUD considers the sum of commitments and expenditures from the fiscal year allocation being examined and later allocations.

² Fiscal year 2006 HOME funds that were not spent by September 30, 2013, were subject to recapture by the United States Treasury.

³ Program income and recaptured funds may result from the resale and recapture requirements imposed by HUD and the participating jurisdiction on the participants to ensure affordability during predetermined periods, depending on the assistance amount provided.

The Municipality's Department of Housing is responsible for administering the HOME program. Its books and records are maintained at Amadeo Street, Carolina, PR. We selected the Municipality of Carolina for review as part of the HUD Office of Inspector General's (OIG) strategic plan, based on the amount of HOME funds approved.

The objectives of the audit were to determine whether HOME-funded activities met program objectives, home buyers complied with HOME's primary residency requirement for the duration of the period of affordability, and the Municipality maintained a financial management system in compliance with the U.S. Department of Housing and Urban Development's (HUD) requirements and reported accurate and supported information in HUD's Integrated Disbursement and Information System.

RESULTS OF AUDIT

Finding 1: HOME-Funded Activities Did Not Meet Program Objectives

The Municipality disbursed HOME funds for three activities that showed signs of slow progress without assurance that the activities would generate the intended benefits. In addition, it did not ensure that the principal residency requirement was met for the duration of the period of affordability for 35 home buyers. These deficiencies occurred because the Municipality did not implement adequate procedures and controls to ensure that its activities met HOME objectives and disregarded HUD's requirements. As a result, HUD had no assurance that more than \$8.2 million disbursed for HOME-funded activities met program objectives and fully provided the intended benefits.

Slow Progress Activities

The Municipality disbursed more than \$7.5 million for three activities that reflected slow progress without assurance that the activities would provide the intended benefits. HUD regulations at 24 CFR (Code of Federal Regulations) 92.504(a) provide that the Municipality is responsible for managing the day-to-day operations of its HOME program, ensuring that HOME funds are used in accordance with all program requirements and written agreements, and taking appropriate action when performance problems arise.

Felipe Birriel housing project – The activity was initially funded on June 23, 2003, for land acquisition and construction of a 60-unit housing project to be sold to low- and very low-income families. In 2011, the scope of the housing project was reduced to 56 units due to an archeological discovery at the project site. In June 2013, the Municipality decided that only 28 of the 56 units to be constructed would be subsidized with HOME funds.

We performed a site inspection of the housing project in September 2013 and confirmed that the project was not finished. The construction of the housing project started in May 2013, and at the time of our inspections, none of the HOME-subsidized units had been completed. See project picture below.



Figure 1-Felipe Birriel housing project

More than 10 years had elapsed since HOME funds were committed to the activity, and the intended benefits had not materialized. HUD's information system showed that the Municipality had obligated more than \$4.2 million in HOME funds, representing an investment of more than \$153,000 per unit. As of February 2014, the Municipality had disbursed more than \$3.9 million, or 92 percent of the total funding, but the project had not been completed. Based on this condition, HUD had no assurance that the Felipe Birriel housing project would fully meet HOME program objectives and provide the intended benefits. Therefore, more than \$3.9 million disbursed was unsupported.

Lorenzo Vizcarrondo housing project – The activity was initially funded on July 28, 2004, for land acquisition and construction of a 33-unit housing project to be sold to low- and very low-income families. HUD's information system showed that the Municipality obligated more than \$3.8 million in HOME funds for this activity.

We performed a site inspection of the housing project in July 2013 and confirmed that the construction of the project had not started. See project picture below.



Figure 2-Lorenzo Vizcarrondo housing project site

More than 9 years had elapsed since HOME funds were committed to the activity, and the intended benefits had not materialized. Based on this condition, HUD had no assurance that the Lorenzo Vizcarrondo housing project would fully meet HOME program objectives and provide the intended benefits. Therefore, more than \$2.8 million in HOME funds disbursed was unsupported.

Federico Cordero housing project – The activity was initially funded on April 20 2007, for land acquisition and construction of a 36-unit housing project, of which 18 units were to be sold to low- and very low-income families and subsidized with HOME funds. HUD’s information system showed that the Municipality drew down more than \$2 million in HOME funds for this activity. According, to the Municipality’s records, the project was completed on April 2013.

We performed a site inspection of the housing project in October 2013 and found that 7 of the 18 HOME-subsidized units had not been sold and occupied by low- and very low-income families. Based on this condition, HUD had no assurance that the Federico Cordero housing project would fully meet HOME program objectives and provide the intended benefits. Therefore, more than \$700,000 in HOME funds disbursed was unsupported.

The Municipality did not properly manage activities to ensure compliance with HOME program objectives. Program regulations at 24 CFR 92.2 provide that in projects owned by a participating jurisdiction, the funds should be committed and the project should be set up in HUD’s information system when construction can reasonably be expected to start within 12 months of the project setup date. More than 7 years had elapsed since HOME funds were committed to the three activities, and the intended benefits had not materialized.

Principal Residency Requirement Not Supported

The Municipality provided more than \$675,000 in home-buyer assistance without making appropriate monitoring efforts to ensure that home buyers met the HOME principal residency requirement in 24 CFR 92.254(a)(3). Internal monitoring reviews initiated in March 2012 identified 35 home buyers that did not comply with HOME’s primary residency requirement for the duration of the period of affordability. For example, in some cases, the owner did not reside in the unit, the unit was leased to another person, or the unit was vacant because it had been repossessed by the bank. Appendix C provides details on the 35 home buyers.

Contrary to requirements in 24 CFR 92.504(a), the Municipality did not ensure that home buyers complied with all program requirements and did not take appropriate measures when performance issues arose. In all cases, more than 1

year had elapsed since the Municipality became aware that the intended benefits had not occurred without making appropriate monitoring efforts. The Municipality's HOME program director informed us that the Municipality was aware of the home buyers who did not comply with the principal residency requirement but no further action was taken because of the lack of staff and resources. This was not an acceptable explanation for not performing an integral component of the Municipality's HOME program responsibilities and disregarding HUD's instructions and requirements.

A June 2011 HUD monitoring included a similar deficiency, and HUD urged the Municipality to establish procedures to ensure compliance with the principal residency and affordability requirements. However, the deficiency remained unresolved.

Section VII of Notice CPD 12-003 provides that it is the Municipality's responsibility to ensure that the HOME-assisted housing qualifies as affordable housing during the period of affordability. If the original home buyer no longer occupies the unit as his or her principal residence, the Municipality, as the entity responsible for the day-to-day operations of its HOME program, must repay its investment trust account from non-Federal funds. The Municipality did not enforce the residency requirement and did not reimburse the HOME program when it became aware of the noncompliance. Thus, it did not adequately manage these activities to ensure that \$675,194 in HOME assistance provided met program objectives and fully provided the intended benefits.

Conclusion

The deficiencies discussed above occurred because the Municipality did not implement adequate procedures and controls to ensure that its activities met HOME objectives and disregarded HUD's requirements. As a result, HUD had no assurance that more than \$8.2 million disbursed for HOME-funded activities met program objectives and fully provided the intended benefits.

Recommendations

We recommend that the Director of the San Juan Office of Community Planning and Development

- 1A. Reevaluate the feasibility of the activities and determine the eligibility of the \$7,136,298 disbursed for the three projects with signs of slow progress.⁴ The Municipality must reimburse its HOME program from non-Federal funds if

⁴ Total disbursements of \$7,542,737 were adjusted to consider \$230,811 questioned in recommendation 2A, \$68,322 questioned in recommendation 2B, \$56,102 questioned in recommendation 2D, and \$51,204 questioned in recommendation 2C.

HUD determines the activities to have been terminated and reprogram and put to better use any unexpended funds associated with the terminated activities.

- 1B. Require the Municipality to submit all supporting documentation showing that the 35 home buyers met the principal residency requirement for the duration of the period of affordability or reimburse the HOME program from non-Federal funds the \$675,194 in HOME assistance provided.
- 1C. Recapture any shortfalls generated by the closure and deobligation of funds associated with recommendations 1A to 1B that do not meet statutory requirements for the timely commitment and expenditure of funds pursuant to the National Defense Authorization Act of 1991 and/or Title II of the Cranston-Gonzalez National Affordable Housing Act, as amended.
- 1D. Require the Municipality to fully implement monitoring control procedures and properly follow up on monitoring results to ensure that assisted activities meet program objectives and applicable affordability requirements.

Finding 2: The Municipality’s Financial Management System Did Not Comply With HUD Requirements

The Municipality’s financial management system did not properly identify the source and application of more than \$726,000 in HOME funds and did not support the eligibility of more than \$68,000 in program disbursements. In addition, the Municipality allowed the use of more than \$62,000 for ineligible expenditures, did not remit to its treasury account more than \$56,000 in unexpended drawdowns, and consistently maintained a high cash balance in its bank account. These deficiencies occurred because the Municipality did not set up the appropriate accounts to trace HOME receipts and expenditures and did not implement adequate measures to ensure compliance with program requirements. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for authorized purposes and in accordance with HUD requirements.

Inadequate Accounting Records

The Municipality’s accounting records did not reflect complete and accurate financial information on HOME program activities and did not permit the adequate tracing of program receipts and expenditures. Regulations at 24 CFR 85.20(b) require grantees to maintain financial records that are accurate, current, and complete and that adequately identify the source and application of funds provided for assisted activities. However, the Municipality’s accounting records did not comply with HUD requirements and were not adequate for the preparation of reports. For example, the records maintained did not reflect disbursement by grant, activity, and funding type and did not properly account for capital assets. In two activities, the Municipality’s records reflected that it disbursed more funds than were drawn from HUD’s system. However, the Municipality could not explain the difference or the source of the extra funds. The general ledger accounts did not reflect the correct balance and did not provide individual accounts for the recording of receipts associated with program income, recaptured funds, and repayments. These were all recorded in the same general HOME account.

In addition, for the period July 1, 2011, to October 31, 2013, the Municipality’s accounting records did not reflect the disposition of more than \$495,000 for the HOME program. As of October 2013, HUD’s system reflected that the Municipality had withdrawn more than \$5 million in HOME funds, but analysis of amounts posted in the Municipality’s check register showed just over \$4.5 million in disbursements. See table below.

HUD’s information system drawn amount	\$5,001,054
Municipality’s records disbursed amount	4,505,127
Difference	\$495,927

Table 1

The Municipality also provided conflicting information on the total amount disbursed for HOME-funded activities. For example, the expenditures shown in the Municipality's records for two activities did not agree with amounts reflected in HUD's information system, and the Municipality could not account for \$230,811 in HUD drawdowns. See table below.

Activity number	Activity Name	Municipality's records	HUD's information system	Difference
403	Lorenzo Vizcarrondo	\$2,611,805	\$2,800,516	(\$188,711)
379	Felipe Birriel	<u>\$2,672,584</u>	<u>\$2,714,684</u>	(\$42,100)
Total		<u>\$5,284,389</u>	<u>\$5,515,200</u>	(\$230,811)

Table 2

The Municipality did not maintain a financial management system that permitted the tracing of funds to a level which ensured that such funds had not been used in violation of the restrictions and prohibitions of applicable statutes. The Municipality could not explain discrepancies between its records and HUD's information system and could not account for \$726,738 drawn. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for eligible purposes.

Unsupported Program Disbursements

Activity delivery costs – The Municipality charged the HOME program more than \$37,000 for project costs associated with wages of two municipal employees. Regulations at 24 CFR 92.206(d)(6) allow disbursements for eligible project costs, including staff and overhead costs directly related to carrying out the project, such as services related to assisting potential owners, tenants, and home buyers. In addition, 24 CFR 92.508(a)(3)(ii) requires participating jurisdictions to maintain records demonstrating the source and application of funds, including supporting documentation, in accordance with 24 CFR 85.20. However, the Municipality did not provide supporting documentation showing the basis and reasonableness of funds charged to HOME activities and how these costs directly related to carrying out the activities. Therefore, HUD lacked assurance of the reasonableness, allowability, and allocability of \$37,501 in project delivery costs charged to the HOME program on June 2013.

Project costs – The Municipality did not support the reasonableness and allowability of more than \$30,000 in HOME program funds disbursed. Regulations at 24 CFR 92.206 and 92.508(a) allow disbursements for reasonable and allowable costs associated with HOME-funded projects, which are supported with records that enable HUD to determine that HOME requirements were met. See table below for details of the unsupported disbursements.

Date	Check number	Amount	Description
Aug. 19, 2004	1539	18,700	Canceled check not provided
May 07, 2004	1483	11,212	Payment related to property appraisals for the Lorenzo Vizcarrondo housing project; no vendor's invoice, evidence of service receipt, etc.
Aug. 12, 2004	1533	909	Canceled check not provided
Total		<u>\$30,821</u>	

Table 3

Ineligible Program Disbursements

The Municipality disbursed \$51,204 in HOME funds for appraisal and blueprint costs that were not related to HOME activities or for activities that were not carried out. In addition, it improperly disbursed \$11,000 in HOME funds to reimburse a 2010 HUD finding. Therefore, the HOME program was charged with unnecessary costs that provided no benefits and did not meet program objectives. See the table below for details of the ineligible disbursements.

Date	Check number	Amount	Description
Apr. 3, 2009	2327	\$27,664	Appraisals and residential inspections in relation to acquisitions that were not carried out
Aug. 10, 2012	2491	11,000	Payment of a HUD finding
Aug. 11, 2005	1730	8,165	Payment for title search, property survey, and registration fees for two lots that were already owned by the Municipality
May 7, 2004	1483	7,475	Payment for title search, property survey, and registration fees unrelated to HOME project
June 27, 2008	2217	7,044	Blueprints related to property acquisitions that were not carried out
Apr. 3, 2009	2333	856	Tax payments to the Puerto Rico Treasury related to a property acquisition not carried out
Total		<u>\$62,204</u>	

Table 4

Unexpended Drawdowns

The Municipality failed to return more than \$56,000 in unexpended HOME drawdowns. HUD regulations at 24 CFR 92.502(c)(2) state that HOME funds drawn down from a participating jurisdiction's treasury account must be expended for eligible costs within 15 days. Any unexpended drawdowns must be returned to HUD. In February 2008, the Municipality received a check totaling \$56,102

associated with the reimbursement of previously funded HOME activities.⁵ The Municipality did not provide supporting documentation showing the disposition of the receipts and whether the funds were returned to its treasury account as required by HUD. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for eligible purposes.

High Cash Balance

HUD regulations at 24 CFR 92.502(c)(3) require that HOME funds in the participant jurisdiction's local account be disbursed before additional grant funds are requested. Contrary to HUD requirements, the Municipality did not disburse HOME funds in a timely manner and consistently maintained a high cash balance in its bank account. The Municipality's December 2013 bank statement reflected a cash balance of more than \$158,000, and the Municipality maintained a monthly average balance of more than \$85,000 during the 18-month period ending December 2013. See figure below.

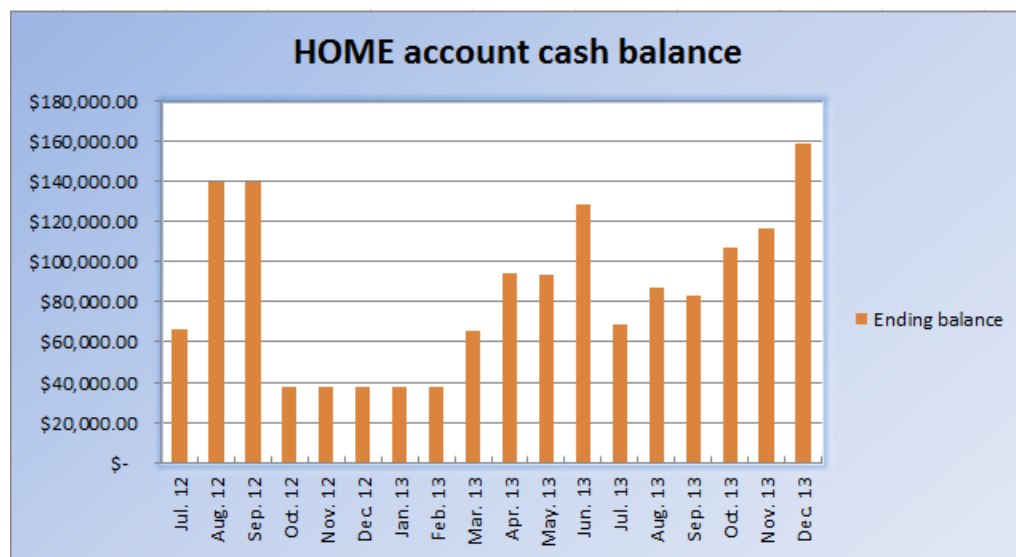


Figure 3

Conclusion

The weaknesses discussed above occurred because the Municipality did not set up the appropriate accounts to trace HOME receipts and expenditures and did not implement adequate measures to ensure compliance with program requirements. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for authorized purposes and in accordance with HUD requirements.

⁵ The State court returned the funds because the expropriation did not take place since the Municipality was already the owner of the property.

Recommendations

We recommend that the Director of the San Juan Office of Community Planning and Development require the Municipality to

- 2A. Submit all supporting documentation showing the eligibility and propriety of \$726,738 in unaccounted for drawdowns from its treasury account or reimburse the HOME program from non-Federal funds.
- 2B. Submit all supporting documentation showing the eligibility and propriety of \$68,322 charged to the HOME program for project and administrative costs or reimburse the program from non-Federal funds.
- 2C. Reimburse from non-Federal funds \$62,204 in ineligible project costs.
- 2D. Remit to its treasury account and put to better use the reimbursed HOME funds totaling \$56,102.
- 2E. Develop and implement a financial management system in accordance with HUD requirements to ensure that HOME funds drawn down can be traced to a level which ensures that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.
- 2F. Develop and implement procedures to ensure that funds are disbursed in a timely manner.

Finding 3: The Municipality Did Not Have Adequate Controls Regarding Information Entered Into HUD's Information System

The Municipality did not ensure the accuracy of commitments and other information entered into HUD's information system. It did not support more than \$387,000 in HOME commitments, failed to report more than \$233,000 in program income receipts, and reported other inaccurate data in HUD's information system. These deficiencies occurred because the Municipality did not properly monitor the accuracy of commitments and other information reported in HUD's information system and was not fully aware of HUD requirements. As a result, HUD had no assurance that the Municipality met HOME program commitment and disbursement requirements.

Unsupported Commitments

The Municipality reported in HUD's information system that it had committed more than \$7.4 million in HOME funds for two housing activities. However, it did not maintain proper records to support more than \$259,000 in reported commitments. The Municipality could not provide a list of the commitments made in relation to the two activities. The only documentation provided was a disbursement register maintained on Excel spreadsheets with the corresponding purchase order number. However, the register was incomplete. The table below shows the activities with overstated commitments.

Activity number	Activity name	Reported commitment amount in HUD's information system	Committed amount per Municipality's records	Overstated commitment
403	Lorenzo Vizcarrondo	\$3,120,130	\$2,931,420	\$188,710
379	Felipe Birriel	<u>4,287,287</u>	<u>4,216,622</u>	<u>70,665</u>
Total		<u>\$7,407,417</u>	<u>\$7,148,042</u>	<u>\$259,375</u>

Table 5

The Municipality also failed to reprogram and put to better use more than \$128,000 in unexpended obligations associated with a terminated housing activity. HUD's regulations at 24 CFR 92.205(e) provide that a HOME-assisted project that is terminated before completion, either voluntarily or otherwise, constitutes an ineligible activity. Therefore, HOME funds invested in the project must be repaid and unexpended funds deobligated. On July 23, 2013, the Municipality and HUD reached an agreement for the Municipality to repay more than \$1.13 million in HOME funds associated with a terminated activity that was not completed. More than 6 months had elapsed since the repayment plan with HUD was signed, and as of January 24, 2014, the activity had unexpended obligations that had not been reprogrammed and put to better use.

The Municipality did not properly monitor the accuracy of information reported in HUD's information system, allowing commitments to be overstated by at least

\$387,449. The inaccurate data compromised the integrity of HUD's information system and the degree of reliability that could be placed on the data for monitoring commitments and compiling national statistics on the HOME program.

Program Income and Recaptured Funds Not Properly Reported

Contrary to HUD requirements, the Municipality did not report proceeds of more than \$233,000 in program income and recaptured funds in HUD's information system. HUD's regulations at 24 CFR 92.503 provide that program income, recaptured funds, and repayments received must be deposited into the participating jurisdiction's HOME account to carry out eligible activities. These receipts must be reported in HUD's information system and used before additional HOME withdrawals are made as required at 24 CFR 92.502(c)(3).

The Municipality's records showed that it received more than \$1.3 million in program income and recaptured funds from July 1, 2001, through June 30, 2013. However, as of June 30, 2013, the Municipality had reported only \$1.07 million in HUD's information system, and \$233,137 remained unreported. Therefore, the Municipality did not report program income and recaptured funds in HUD's information system in a timely manner. The Municipality did not properly monitor the accuracy of the program income and recaptured funds reported in HUD's information system, resulting in an understatement of at least \$233,137 in program receipts.

Other Deficiencies

Inaccurate commitment dates – In two activities, the Municipality reported in HUD's information system the commitment of more than \$7.4 million in HOME funds between 166 and 362 days after the grant agreement was executed. Therefore, the actual commitment data were reported in HUD's information system with significant delays and inaccurate commitment dates. In addition, neither contract mentioned the projects by name. As a result, the requirement in 24 CFR 92.2 for an identifiable project at the time of initial commitment in HUD's information system was unsupported.

Inaccurate number of housing units – In two activities, the Municipality did not report accurate activity descriptions in HUD's information system. The Municipality reported the construction of 100 total units for a project when the project had only 56 units. For another project, the description stated that the project would consist of 20 units, when the documentation indicated that there were 33 units.

Undated signatures in agreements – For 12 written agreements reviewed, the Municipality did not implement adequate controls to ensure compliance with Section VII of Notice CPD 07-06. This notice required that signatures of all parties be dated to show the execution date. A Municipality official informed us that he was unaware of this requirement. As a result, HUD had no assurance of the actual commitment date and the Municipality's compliance with HUD's commitment requirements.

Conclusion

These deficiencies occurred because the Municipality did not properly monitor the accuracy of commitments and other information reported in HUD's information system and was not fully aware of HUD requirements. The inaccurate data compromised the integrity of HUD's information system and the degree of reliability that could be placed on the data for monitoring commitments and compiling national statistics on the HOME program. As a result, HUD had no assurance that the Municipality met HOME program commitment and disbursement requirements.

Recommendations

We recommend that the Director of the San Juan Office of Community Planning and Development require the Municipality to

- 3A. Deobligate, reprogram, and put to better use \$387,449 in overstated commitments.
- 3B. Correct any inaccurate information in HUD's information system, including but not limited to the receipt of \$233,137 associated with program income and recaptured funds not reported and inaccurate commitment amounts and dates.
- 3C. Develop and implement controls and procedures to ensure that only valid commitments are reported to HUD.
- 3D. Develop and implement procedures to ensure that program income and recaptured funds are properly reported.
- 3E. Develop and implement procedures to ensure that accurate information on HOME-funded activities is reported in HUD's information system.
- 3F. Develop and implement procedures to ensure that grant agreements are properly signed and dated.

SCOPE AND METHODOLOGY

The objectives of the audit were to determine whether HOME-funded activities met program objectives, home buyers complied with HOME's primary residency requirement for the duration of the period of affordability, and the Municipality maintained a financial management system in compliance with the U.S. Department of Housing and Urban Development's (HUD) requirements and reported accurate and supported information in HUD's Integrated Disbursement and Information System.

To accomplish our objectives, we

- Reviewed applicable HUD laws, regulations, and other HUD program requirements;
- Interviewed HUD and Municipality officials;
- Obtained an understanding of and reviewed the Municipality's controls and procedures as they related to our objectives;
- Reviewed monitoring internal reviews and independent public accountant and HUD's information system reports; and
- Reviewed and traced information reported in HUD's information system to the Municipality's records, including program income and disbursement records.

HUD's information system reflected that the Municipality had six open HOME-funded activities with commitments of more than \$16.5 million as of October 31, 2013. We selected and reviewed five activities with commitments totaling more than \$15.3 million, based on funding amounts and indications of slow progress. We reviewed the five activities to determine the status of activities, for which HOME funds had been disbursed but which reflected slow progress.

The Municipality conducted six monitoring reviews, between March and June 2012. The reviews identified 35 home buyers who did not comply with HUD's principal residency requirement for the duration of the period of affordability. For these home buyers, the Municipality provided \$675,194 in HOME program assistance. We reviewed the 35 home buyers to determine whether the Municipality made proper monitoring efforts to ensure that activities met program objectives and fully provided the intended benefits.

The Municipality's accounting records reflected that it disbursed more than \$4.5 million in HOME funds between July 1, 2011, and October 31, 2013. We selected and reviewed disbursements with amounts greater than \$100,000 and based on the type of disbursement or vendor. The sample resulted in 30 disbursements totaling more than \$3.7 million. We reviewed

179 additional disbursements totaling more than \$4.7 million that were made between January 2003 and December 2010, based on deficiencies noted regarding the allocation of the charges.⁶ More than \$8.5 million in HOME program expenditures was reviewed to determine whether funds were used for supported and eligible efforts.

We also reviewed the Municipality's HOME program bank statements between July 2012 and December 2013 to determine whether HOME funds were disbursed within HUD's timeframes.

HUD's information system reflected that the Municipality had committed more than \$14.4 million in HOME funds for six activities as of June 27, 2013. We selected for review two activities with commitments totaling more than \$6.3 million. We reviewed these activities to determine whether the information reported to HUD, including commitments, was accurate and supported.

The Municipality's records showed that between July 1, 2001, and June 30, 2013, it received more than \$1.3 million in program income and recaptured funds. We reviewed the Municipality's records associated with the program income receipts to determine whether the funds were properly reported in HUD's information system.

To achieve our audit objectives, we relied in part on computer-processed data contained in HUD's information system. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing and found the data adequate for our purposes. We did not rely on computer-processed data contained in the Municipality's database, nor were the data used to materially support our audit findings, conclusions, and recommendations. We did not select 100 percent of the items for testing as the selections made provided sufficient evidence for the findings presented. The results of the audit apply only to items selected for review and cannot be projected to the universe or population.

The audit generally covered the period July 1, 2011, through April 30, 2013. However, due to the issues associated with unrecorded program income and activities with signs of slow progress for which more than 7 years had elapsed since its initial funding, we expanded our scope to cover July 1, 2001, through December 31, 2013. We conducted our fieldwork from June 2013 through February 2014 at the Municipality's offices in Carolina, PR.

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 objectives.

⁶ HUD's information system reflected more than \$13.8 million in drawdowns between January 2003 and December 2010.

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:

- Program operations – Policies and procedures that management has implemented to provide reasonable assurance that a program meets its objectives, while considering cost effectiveness and efficiency.
- 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 laws and regulations – Policies and procedures that management has implemented to reasonably ensure that program implementation is consistent with laws and regulations.
- Safeguarding of assets – Policies and procedures that management has implemented to reasonably prevent and promptly detect unauthorized acquisition, use, or disposition of assets and resources.

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 Municipality did not implement adequate procedures and controls to ensure that activities provided the intended benefits and home buyers met affordability requirements (see finding 1).
- The Municipality did not develop and implement a financial management system that complied with HUD requirements (see finding 2).
- The Municipality did not have adequate controls to ensure that accurate information was reported to HUD (see finding 3).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1A		\$7,136,298	
1B		675,194	
2A		726,738	
2B		68,322	
2C	\$62,204		
2D			\$56,102
3A			387,449
Total	<u>\$62,204</u>	<u>\$8,606,552</u>	<u>\$443,551</u>


- 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.
- 2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.
- 3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, if the Municipality implements recommendations 2D and 3A, funds will be available for other eligible activities consistent with HOME requirements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

<p>www.teleservicioiginte.com</p>	<p>ESTADO LIBRE ASOCIADO DE PUERTO RICO GOBIERNO MUNICIPAL AUTÓNOMO DE CAROLINA</p> <p>June 12, 2014</p> <p>Ms. Nikita Irons Regional Inspector General for Audit U.S. Department of Housing and Urban Development Region 4 - Office of Inspector General Office of Audit, Box 42 Richard B. Russell Federal Building 75 Spring Street, SW, Room 350 Atlanta, GA, 30303-3388</p> <p>Subject: Comments to Draft Audit Report The Municipality of Carolina Did Not Properly Administer Its HOME Program</p> <p>Dear Ms. Irons:</p> <p>We appreciate the opportunity to comment on the subject draft Memorandum your Office submitted to our attention on May 28, 2014. As requested by your Office, we completed the review of the document and have prepared the following comments.</p> <p>First, we recommend the OIG to reorganize the report to include at the beginning of the document the different cost deficiencies identified in the document. It is clear that most of the cost deficiencies identified in the report are unsupported cost. The unsupported cost are those costs charged to a HUD-financed or HUD-insured program or activity where the auditor cannot determine eligibility at the time of the audit. This does not means that the Municipality incurred in an illegal action or practice. As explained in detail in this letter for all the unsupported cost recommendation we included additional information that will lead to the closing of the finding without any financial consequence for the Municipality. If possible we request that the OIG includes the definitions of cost included in Appendix 1 into the Highlights section of the report. This will allow the reader to be aware of cost category and the actual severity of the finding or recommendation.</p> <p>As explained to members of your staff during the exit conference the Municipality of Carolina is committed to comply with all the applicable federal regulations.</p> <p></p> <p>P.O. Box 8, Carolina, Puerto Rico 00986-0008 ● (787) 757-2626 ● Teleservicios: 641-2000 ● 641-0958</p>
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The following are the specific comments to the each of the recommendations included in the report.

FINDING #1- HOME-FUNDED ACTIVITIES DID NOT MEET PROGRAM OBJECTIVES

Recommendation 1A. Reevaluate the feasibility of the activities and determine the eligibility of the \$6,201,882 disbursed for the three projects with signs of slow progress. The Municipality must reimburse its HOME program from non-Federal funds if HUD determines the activities to have been terminated and reprogram and put to better use any unexpended funds associated with the terminated activities.

Comment:

The three projects identified by the OIG in the report are included in a master plan for the redevelopment of the traditional urban center of Carolina. This redevelopment plan was established for the purpose of stabilizing down community that have suffered from foreclosures and abandonment and to provide low income families with housing that is safe, sound and sanitary. Providing quality housing for people of all income levels is an integral component of the Municipal Administration of Carolina. Our administration is committed to create walkable neighborhoods with access to public transportation, parks and civic spaces. The plan is consistent with HUD's Public Policy.

HUD's has recognized that downtown revitalization is a complex process. The process includes compliance with environmental and historical requirements, acquisition, relocation, parcel aggregation, construction and marketing. All this issues has an impact on cost and schedule because of the uncertainty.

In 2005 the Municipality received the Robert L. Woodson Jr. Award from HUD for the action taken to remove regulatory barriers for the development of low income Housing. The award considered some of the projects included in this finding. According to HUD the award was based on the following:

"Municipalities in Puerto Rico operate in a regulatory environment totally different from those found on the U.S. mainland. In most cases, the Commonwealth of Puerto Rico is directly involved in the process of providing many of the required permits and approvals for building construction and rehabilitation. As a result, getting approval to build or restore affordable housing tends to be slow, costly and unresponsive. Taking advantage of new legislation, the Carolina Municipal assumed almost all of the regulatory responsibilities for housing development. Combining regulatory reform with innovative financing and other incentives, affordable housing construction increased from 400 units between 1992 and 2000, to 1,000 units between 2001 and 2004." (HUD Press Release Robert L. Woodson Jr. Awards-<http://archives.hud.gov/news/2005/pr05-092.cfm>.)

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Comment 1

Comment 2

The eligible projects evaluated by the OIG appeared to be progress at a slow pace, but they were developing at the typical pace of similar projects in Puerto Rico and the United States. Although the current regulations establishes strict deadline for commitment and completion of the projects, the applicable regulation when the projects were planned did not. It must be understood that for these projects the Municipality is in compliance with the applicable HOME program regulations.

Federico Cordero Project

All the cost incurred by the Municipality are eligible and permitted by the HOME program regulations. The following table is the layering analysis of the project and the eligibility category of cost paid with HOME funds:

	Total	HOME Municipal	Eligibility
1. Acquisition	\$ 2,052,720.46	\$ 653,020.56	24 CFR 92.205 (a)(1)
2. Hard Costs			
Demolition/Site Clearance	\$ 150,125.00	\$ 150,125.00	24 CFR 92.205 (a)(1)
Construction	\$ 4,246,270.90	\$ 1,006,270.90	24 CFR 92.205 (a)(1)
3. Soft Costs			
Soft Costs	\$ 25,000.00	\$ 25,000.00	24 CFR 92.206(d)
Architecture/Engineering	\$ 173,690.08	\$ 173,690.08	24 CFR 92.206(d)
Survey			
Total Project Costs	\$6,648,096.44	\$2,008,306.54	

As the table shows the HOME funds were incurred in eligible cost permitted by the regulation.

As recognized by the audit the 36 unit's project was completed and the occupancy process is underway. Since the visit of the OIG the Municipality continued with the occupancy of the project and as of the day of this letter the 16 of the 18 HOME assisted units are occupied and the performance data was entered into IDIS(evidence is provided as attachment 1 of this letter(copy of mortgages and IDIS screens).

The following table shows each of the occupied HOME assisted unit in the project and the occupancy date:

UNIT	CLOSING DATE
3-306	5/30/2013
1-101	5/30/2013
2-210	5/30/2013
1-305	5/30/2013
2-107	5/30/2013
2-113	5/30/2013
2-216	6/26/2013

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2-101	7/30/2013
1-210	8/20/2013
2-204	8/20/2013
1-204	10/8/2013
2-905	11/20/2013
2-311	12/23/2013
1-311	11/4/2013
3-203	2/11/2014
1-107	2/11/2014
2-317	
3-102	

The two remaining unit in the project are optioned and are awaiting the approval of the mortgage bank (see [attachment 2](#)).

Based on the facts and actual condition of the project we determined that the final occupancy and completion of the Federico Cordero Project is feasible.

We expect to complete the occupancy of the project by June 30, 2014. Based on the information presented we can assure that the Federico Cordero housing project fully meet HOME program objectives and provides its intended benefits.

Felipe Birriel Project

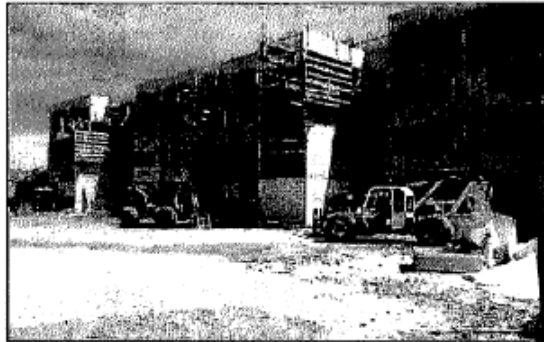
All the cost incurred by the Municipality are eligible and permitted by the HOME program regulations. The following table is the layering analysis of the project and the eligibility category of cost paid with HOME funds:

	Total	HOME Municipal	Eligibility
1. Acquisition	\$2,359,910.46	\$2,359,910.46	24 CFR 92.205 (a)(1)
2. Hard Costs			
Demolition/Site Clearance	\$5,000.00	\$5,000.00	24 CFR 92.205 (a)(1)
Construction	\$1,273,232.29	\$1,273,232.29	24 CFR 92.205 (a)(1)
3. Soft Costs			
Soft Costs	\$14,623.57	\$14,623.57	24 CFR 92.206(d)
Architecture/Engineering	\$255,896.75	\$255,896.75	24 CFR 92.206(d)
Survey			
Total Project Costs	\$3,908,663.07	\$3,908,663.07	

As the table shows the HOME funds were incurred in eligible cost permitted by the regulation.

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The auditors recognized in the report that the project is being constructed and that 92% of the funds has been committed for its construction. Since the visit of the OIG construction continued and the project is expected to be completed by July 31, 2014. The following photos shows compares how construction has continued and progressed since the OIG visit to the project:



July 31, 2013



June 6, 2014

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It is clear from the photos that the Municipality is working toward the completion of the project but it is necessary to explain why project completion was delayed.

Reasons for delay Felipe Birriel

The Felipe Birriel Project was developed in deteriorated area of downtown Carolina. For the development of the project it was necessary to acquire 29 structures, relocated 37 families and demolish the existing structures. Although the site was previously impacted by the previous development it was found that a historic cemetery was located in the area. This required additional consultation with the State Historic Preservation Office. The consultation with SHPO concluded on January 31, 2012 and they required the mitigation of the site, the redesign of the project and the reduction of the number of units to 56 (28 HOME assisted). All of these issues delayed the initiation of construction and increased the construction cost.

Compliance with the National Environmental Protection Act and Uniform Relocation Act is required by the HOME program regulation. Due to unforeseen circumstances the project was required to be redesigned. HUD's must recognize that the project was only feasible if developed by the Municipal Government, because no developer will incur in similar cost to develop a low income project in the downtown area.

We must also state that although progress appear to be slow the project it is in compliance with the regulation of the HOME program and that the Municipality is working toward its completion and the intended benefits will materialized before year end.

Based on the facts and actual condition of the project we determined that completion of the construction and the final occupancy of the Felipe Birriel Project is feasible.

To occupy the project the developer prepared the affirmative marketing plan that is included as attachment 3. Under this plan the pre-sale of the project is planned for late June 2014 and occupancy of the project is expected during the remaining months of the year.

Lorenzo Vizcarrondo

All the cost incurred by the Municipality are eligible and permitted by the HOME program regulations. The following table is the layering analysis of the project and the eligibility category of cost paid with HOME funds:

	Total	HOME Municipal	Eligibility
1. Acquisition	\$2,401,938.67	\$2,401,938.67	24 CFR 92.205 (a)(1)
2. Hard Costs			
Demolition/Site Clearance	15,750.00	15,750.00	24 CFR 92.205 (a)(1)
Construction	\$10,385.42	\$10,385.42	24 CFR 92.205 (a)(1)
3. Soft Costs			
Soft Costs	\$10,262.63	\$10,262.63	24 CFR 92.206(d)
Architecture/Engineering	\$174,878.00	\$174,878.00	24 CFR 92.206(d)
Survey			
Total Project Costs	\$2,613,214.72	\$2,613,214.72	

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As the table shows the HOME funds were incurred in eligible cost permitted by the regulation.

Like the other two project described before Lorenzo Vizcarrondo project is located on a formerly dilapidated urban area of downtown Carolina. The project also required the acquisition, relocation, and demolition to be completed before new construction. After the demolition of the unit the archaeologist on site discovered a 19th century archaeological site. Pursuant to 36 CFR Part 800 the Municipality consulted with SHPO and the Advisory Council on Historic Preservation. As required by the regulation the Municipality negotiated a Memorandum of Understanding that will permit the initiation of the construction of the project. The terms of the MOU (included as attachment 4) requires the completion of a Phase III archaeological report and the curation of the archaeological artifacts. The schedule included in the MOU project that the Phase III archaeological report will be completed by April 2015 and construction is expected to be started by July, 2015. Project construction is expected to be completed by July 2017. Although substantially delayed the Municipality understands that the project is necessary and vital for the downtown master plan and that its completion is feasible.

It is a fact that the project is delayed but the Municipality took multiple action in order to expedite the process including the following:

- Restructured local planning and local permitting with specific timetables reducing approval times from six months to 10-15 days; The local permits for the project were obtained conditioned to the completion of the federal requirements;
- The municipality waived permit fees for the project;
- The Municipality granted the land free of cost, consolidated multiple small lots to form a larger parcel, and then released the property for development;

Even tough the above actions reduced the planning and/or project cost compliance with federal environmental requirements hindered the process and are the actual reasons for the delay.

Recommendation 18. Require the Municipality to submit all supporting documentation showing that the 35 home buyers met the principal residency requirement for the duration of the period of affordability or reimburse the HOME program from non-Federal funds the \$675,194 in HOME assistance provided.

Response:

We must clarify that the Municipality monitored all HOME projects assisted for compliance with 24 CFR 92.254(a)(3). Indeed the 35 cases included in the audit report were identified by the Municipality during a previous monitoring process. Due to changes in program staff the Municipality was unable to verify the residency of the cases identified during the monitoring process. Before the completion of the audit we revisited the projects and requested documentation from the participants. The following table shows the status of the review by project:

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Project	Apartment #	Status
San Ciprian III	111	Compliance
San Ciprian III	304	Compliance
San Ciprian III	309	Review Underway
San Ciprian III	314	Compliance
San Ciprian III	318	Compliance
San Ciprian II	107	Compliance
San Ciprian II	109	Compliance
San Ciprian II	112	Review Underway
San Ciprian II	114	Compliance
San Ciprian II	203	Compliance
San Ciprian II	210	Compliance
San Ciprian II	211	Compliance
San Ciprian II	214	Compliance
San Ciprian II	215	Compliance
San Ciprian II	305	Compliance
San Ciprian II	310	Compliance
San Ciprian II	313	Review Underway
San Ciprian II	314	Compliance
San Ciprian II	315	Compliance
San Ciprian II	316	Compliance
San Ciprian II	317	Review Underway
Balcones de Carolina	O3-301	Compliance
Balcones de Carolina	A3-301	Compliance
Balcones de Carolina	B3-402	Compliance
Balcones de Carolina	C3-402	Review Underway
Balcones de Carolina	E3-401	Compliance
Balcones de Carolina	F3-302	Review Underway
Balcones de Carolina	I3-401	Review Underway
Balcones de Carolina	K3-302	Compliance
Balcones de Carolina	D3-101	Review Underway
Balcones de Carolina	D3-201	Compliance
Balcones de Carolina	D3-401	Compliance

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Project	Apartment #	Status
Balcones de Carolina	I3-302	Compliance
Balcones de Carolina	O3-202	Review Underway
Balcones de Carolina	O3-302	Compliance

As attachment 5 of this letter we are including the supporting documentation that evidences the HOME Assisted Participants are occupying the housing units as required by 92.254(a)(3). If any of the cases are found in noncompliance we will refer them to the legal division in order to enforce the appropriate corrective or legal action.

Recommendation 1C. Recapture any shortfalls generated by the closure and deobligation of funds associated with recommendations 1A to 1B that do not meet statutory requirements for the timely commitment and expenditure of funds pursuant to the National Defense Authorization Act of 1991 and/or Title II of the Cranston-Gonzalez National Affordable Housing Act, as amended.

Response:

Funding for the six (6) projects identified on recommendation 1A and 1B were committed and expended in accordance with the National Defense Authorization Act of 1991 and/or Title II of the Cranston-Gonzalez National Affordable Housing Act.

National Defense Act

We reviewed each of the project to determine the applicability of the NDA requirements. It is necessary to clarify that HUD's HOME Facts Vol. 2 No. 2, February, 2009 establishes that "since the FY 2002 HOME appropriation was the first time HOME funds had an identified three-year period of availability subject to the National Defense Authorization Act, FY 2002 HOME grants are the first HOME funds subject to the expenditure deadlines of that Act". Taking that into consideration we reviewed each of the project and present the results of the analysis in the following table:

Project	Allocation PY	Funding	Analysis
Balcones de Carolina	2001	\$424,263.50	The NDA does not apply to this program year
San Ciprian II	1997	\$2,620,411.61	The NDA does not apply to this program year
San Ciprian III			
Felipe Birriel	2002	\$3,270,407.21	Compliance
Federico Cordero	2006	\$1,962,678.07	Compliance
Lorenzo Vizcarrondo	2003	\$3,111,524.17	Compliance

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HUD's calculates compliance with the Defense Act taking into consideration disbursements in IDIS. IDIS uses a First-In First-Out (FIFO) technique for both committing funds to activities and drawing funds. This means that funds are committed and drawn from the "oldest" available funds first. Based on this technique the Municipality has complied with the on-time disbursement of the funds.

In addition to our review we evaluated the HOME Expiring Funds Reports provided by HUD available at <http://www.hud.gov/offices/cpd/affordablehousing/reports/expiringfunds.cfm>. The reports provided by HUD identify each PJ that has a grant balance that will trigger the application of the NDA. Our review disclosed that none of the project evaluated by the OIG were included in the HOME Expiring Funds Reports.

Based on the review performed we can conclude that all the projects evaluated by the OIG are in compliance with the National Defense Act.

Title II of the Cranston-Gonzalez National Affordable Housing Act.

The HOME program establishes strict requirements regarding the time required for the commitment and disbursement of funds provided for the development of affordable housing. The regulation states that the Participating Jurisdictions (PJs) lose their right to HOME funds that are not committed within 24 months or not disbursed after the five year expenditure deadline.

It is a fact that the Municipality of Carolina has complied with the commitment and disbursement deadlines and requirements. For each of the activity we have completed the setup in IDIS, or executed the required agreements and disbursed the funds in compliance with the applicable rules of the HOME program.

To monitor compliance with the requirement of the Act HUD provided commitment and expenditures deadlines reports. We reviewed each of the report found that the Municipality complied with the requirements of the act. Again we must establish that the calculation of the commitment and expenditures deadlines are aggregated and not project based.

Based on the review performed we can conclude that all the projects evaluated by the OIG are in compliance with the Title II of the Cranston-Gonzalez National Affordable Housing Act.

1D. Require the Municipality to fully implement monitoring control procedures and properly follow up on monitoring results to ensure that assisted activities meet program objectives and applicable affordability requirements.

Response:

We revised the monitoring procedures of the HOME program in order to implement internal controls to assure follow up on monitoring results. A copy of the procedures are included as **attachment 6**.

FINDING #2- THE MUNICIPALITY'S FINANCIAL MANAGEMENT SYSTEM DID NOT COMPLY WITH HUD REQUIREMENTS

Recommendation 2A. Submit all supporting documentation showing the eligibility and propriety of \$741,139 charged to the HOME program for project and administrative costs or reimburse the program from non-Federal funds.

Response:

As required by HUD we are providing with this letter copies of the requested documentation that will allow the OIG to determine the eligibility and the propriety. The following table summarizes the information provided with this letter:

Date	Check number	Amount	Information Provided
Dec. 07, 2005	1797	\$663,000.00	Copy of the appraisal report, voucher, cancelled check, ordinance, and CRIM appraisal. (See Attachment 7)
Aug. 19, 2004	1539	\$18,700.00	Copy of bank statement. Copy of the check was requested to the banking institution and will be submitted as soon as provided to the Municipality. (See Attachment 8)
May 07, 2004	1483	\$11,213.00	Payment related to property appraisals for the Lorenzo Vizcarrondo housing project; no vendor's invoice, evidence of service receipt, etc. (See Attachment 9)
Sept. 09, 2004	1550-B	\$5,020.00	The actual check number is 1550. The letter b identifies the project. Copy of the cancelled check, disbursement documentation. (See Attachment 10)
Jan. 23, 2007	1930	\$2,160.00	Copy of bank statement. Although the bank statement include a copy of the check we requested a clearer copy. When we receive the check we will submit it for review. (See Attachment 11)
Mar. 18, 2010	transfer	\$1,556.00	Copy of the wire transfer from Banco Popular, evidence of the transfer from the Banco Popular to PR Treasury Department (Hacienda) (See Attachment 12)
Aug. 12, 2004	1533	\$909.00	Copy of bank statement. Copy of the check was requested to the banking institution and will be submitted as soon as provided to the Municipality. (See Attachment 13)
Dec. 17, 2003	1521	\$775.00	Copy of the check is included for review. (See Attachment 14)
Sept. 10, 2004	1550-B	\$155.00	The actual check number is 1550. The letter b identifies the project. Copy of the cancelled check, disbursement documentation. (See Attachment 10)
Mar. 18, 2010	transfer	\$150.00	Copy of the wire transfer from Banco Popular, evidence of the transfer from the Banco Popular to PR Treasury Department (Hacienda) (See Attachment 12)
Total		\$703,638.00	

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Comment 8

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Comment 9

In addition to the above cost the OIG requested documentation evidencing \$37,000 for project costs associated with wages of two municipal employees. We certify that the staff paid with HOME funds was carrying out eligible activities of the HOME program as permitted by program regulation and CPD notice 06-01. Due to the fact that the staff was performing duties only to the HOME program no time allocation tracking was necessary. The notice does not require the preparation of a cost allocation nor a time allocation. CPD notice 06-01 establishes that 100% of the staff and overhead costs directly related to carrying out a project, including certain fair housing and housing counseling activities can be charged as project-related soft costs. Based on this notice we distributed the staff and overhead costs equally among all participant served. Yet we understand that it would be adequate to establish a documented cost per services provided to each case. As explained during the exit conference we will present the documentation that evidences how the staff performed duties among the different eligible activities and that the cost were reasonable. We believe that in a time of limited funding the Municipality will continue to charge project related soft costs to the different projects and activities and that HUD must provide additional guidelines on the subject.

Comment 10

Recommendation 2B. Submit all supporting documentation showing the eligibility and propriety of \$726,738 in unaccounted for drawdowns from its treasury account or reimburse the HOME program from non-Federal funds.

Response:

All HOME funds disbursed by the Municipality are accounted and documented and registered in the financial system. Our accounting records are accurate, current, complete, and the financial reporting is free of material misstatements as expressed in the Independent public account report. After reviewing the draft report we found that some of the IDIS report used by HUD included revised vouchers. For example if the auditors used an IDIS PR07 report for the calculation of the disbursement the list will include revised and completed vouchers. In order to obtain correct information the data in the report must be adjusted to remove all duplicated vouchers, if not adjusted the final calculation will yield incorrect values. Although is not clear if that is the situation described by the OIG we will review all the drawdowns of the period from July 1, 2011, to October 31, 2013 and will compare them to the payments made by the Municipality. We will submit the result of the review by October 31, 2014.

Comment 11

Recommendation 2C. Remit to its treasury account and put to better use the reimbursed HOME funds totaling \$317,701.

Response:

Enclosed you will find evidence that the Municipality reimbursed the \$317,701 identified by the OIG. The first reimbursement to the line of credit occurred on October 1, 2010. As attachment 15 we are including the evidence of reimbursement that includes: the Wire Transfer, Voucher Payment, Memorandum from the Finance Director, copy of the IDIS screen recognizing the receipt of the voucher. Based on this information we request the revision of the report to remove this transaction.

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Comment 12

The second reimbursement occurred on March 7, 2008. For this transaction the Municipality deposited the funds in the local HOME account as demonstrated by the evidence included as **attachment 16**.

Both transactions demonstrate that the Municipality complied with the regulation related to the recapture or reimbursement to the HOME investment account.

Although the report establishes that the funds were required to be returned to its treasury account this is not correct. According to HUD: *"The general rule is that HUD grantees and subrecipients must disburse program income, rebates, refunds, contract settlements, audit recoveries and interest earned on any of these funds before requesting additional cash payments from the U.S. Treasury."* (Show Me the Money Page 5-11). In addition to this the HOME program regulation (24 CFR 92.500(c)) establishes that any repayments or recaptured funds must be deposited in the local account.

Based on the evidence presented and the requirement of the regulations we request the elimination of this recommendation.

Comment 13

Recommendation 2D. Reimburse from non-Federal funds \$62,204 in ineligible project costs.

Response:

According to the recommendation and the information included in page 12 of the draft report the Municipality "improperly disbursed \$11,000 in HOME funds to reimburse a 2010 HUD finding". We disagree with this statement because is incorrect and not supported. According to the records included as **attachment 17**, on March 30, 2012 the Municipality transferred the \$11,000 (the total amount transferred was \$20,000) from the local funds account to the HOME program account. This amount is evidenced by the bank statements of both bank accounts (Municipal and HOME Program).

After the funds were received in the HOME program account as required by 24 CFR 92.500© they were transferred to the HOME program Line of Credit. From the HOME program bank account the funds were transferred to HUD and recorded as voucher number 5469790. In addition the funds were put better use by using them in activity 375. The final transaction was recorded on September 12, 2012. At the evidence show the Municipality used local funds to reimburse the HOME program account.

Regarding the remaining items the Municipality will set aside in the next program year municipal budget the \$51,204 to be used for the reimbursement to the HOME program line of credit.

Comment 14

Recommendation 2E. Develop and implement a financial management system in accordance with HUD requirements to ensure that HOME funds drawn down can be traced to a level which ensures that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.

Comments to Draft Audit Report
The Municipality of Carolina Did Not Properly
Administer Its HOME Program

Response:

When the auditors performed the field work the Municipality was undertaking changes to the Electronica Financial Management System (SAP). During the audit period the Municipality was managing transition to the new computerized system while still maintaining some records in the old system. This situation can explain the confusion of some of the reports and information presented to the auditors. The implementation of the new system was completed on April 1, 2014. The new system produces the required detailed reports with the level of information expected by HUD. This new system facilitate the reconciliation of the federal system with the local financial system and the tracing of the fund from source to its application.

2F. Develop and implement procedures to ensure that funds are disbursed in a timely manner.

Response:

As required by HUD a new procedure was created that will ensure that funds are disbursed in a timely manner. The Procedure is included as **attachment 18**.

**FINDING 3: THE MUNICIPALITY DID NOT HAVE ADEQUATE CONTROLS REGARDING INFORMATION
ENTERED INTO HUD'S INFORMATION SYSTEM**

Recommendation 3A. Deobligate, reprogram, and put to better use \$387,449 in overstated commitments.

Response:

We are aware of the recommendation of the OIG and we are working with the San Juan field office staff in the process of deobligation of funds from the activities reviewed by the OIG.

Recommendation 3B. Correct any inaccurate information in HUD's information system, including but not limited to the receipt of \$233,137 associated with program income and recaptured funds not reported and inaccurate commitment amounts and dates.

To avoid the recurrence of the situation the Municipality created a new procedure that will facilitate the management of the program income received by the Municipality. The basics of the new procedure was the creation of a separate bank account in which all program income received will be deposited. The new procedure is included as **attachment 19**.

Since the auditors identified this condition we took immediate action to correct the situation. Enclosed (see **attachment 20**) you will find an IDIS PR09 report that shows the receipt and reuse of the HOME Program Income.

Comment 14

Comment 14

Comment 14

Comments to Draft Audit Report
The Municipality of Carolina Did Not Properly
Administer Its HOME Program

Comment 14

Recommendation 3C. Develop and implement controls and procedures to ensure that only valid commitments are reported to HUD.

Response

This issue is addressed in a new Financial Management Procedure that is included as **attachment 18** for your review.

Comment 14

Recommendation 3D. Develop and implement procedures to ensure that program income and recaptured funds are properly reported.

Response

A new procedure was created and is included as **attachment 19**.

Comment 14

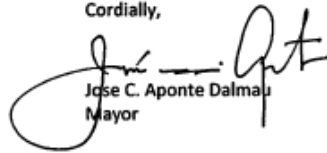
Recommendation 3E. Develop and implement procedures to ensure that accurate information on HOME-funded activities is reported in HUD's information system.

Response:

This issue is addressed in a new Financial Management Procedure that is included as **attachment 18** for your review.

Should you need additional information regarding this letter please contact Mr. Daniel Redón García, at your convenience at (787) 757-2626 Ext. 8494.

Cordially,


Jose C. Aponte Dalmau
Mayor

Enclosures

OIG Evaluation of Auditee Comments

Comment 1 The Municipality stated that the HOME projects appeared to be progressing at a slow pace; however, this was the typical pace of similar projects in Puerto Rico and the United States. In addition, it stated that the Municipality was in compliance with the applicable HOME program regulations at the time the projects were planned.

We do not agree with the Municipality since more than 9 years had elapsed since HOME funds were committed, the intended benefits had not materialized, and HOME funded activities had not met program objectives. Program regulations at 24 CFR 92.2 provide that in projects owned by a participating jurisdiction, the funds should be committed and the project should be set up in HUD's information system when construction can reasonably be expected to start within 12 months of the project setup date. The Municipality did not provide additional documentation showing that projects were in compliance with HOME regulations.

Comment 2 Federico Cordero project - The Municipality indicated that 16 of the 18 HOME-assisted units were occupied and that it provided copies of mortgages and IDIS screens to support its compliance. In addition, it considers the housing project to fully meet HOME program objectives and provide its intended benefits.

Contrary to the Municipality statement, the Municipality did not provide the mortgages for the 16 units, instead copies of grant agreements were provided. The Municipality also did not provide additional documentation to demonstrate that the housing units questioned were occupied by eligible low- and very-low income families. The Municipality must submit appropriate evidence to HUD in order for HUD to make a feasibility determination.

Comment 3 Felipe Birriel project - The Municipality indicated that it considers the housing project to be feasible, that all project costs are eligible, and that the project should be completed by July 31, 2014. In addition, that it prepared a marketing plan and that full occupancy is expected during 2014.

The Municipality must submit the appropriate evidence to HUD demonstrating the feasibility of the project.

Comment 4 Lorenzo Vizcarrondo project - The Municipality stated that the reasons for the delays were the archeological discoveries at the project site. The Municipality indicated that it has entered into a memorandum of understanding with the Puerto Rico State Historic Preservation Society that will permit the construction of the project. It considers the project to be feasible despite the substantial delays. The Municipality expects to commence construction of the project by July 2015 and complete the project by July 2017.

The Municipality must submit the appropriate evidence to HUD demonstrating the feasibility of the project.

Comment 5 The Municipality stated that due to changes in program staff it was unable to follow-up and verify the home buyers' occupancy. In addition, it stated that during the audit it revisited projects and obtained documentation showing that HOME participants were occupying the units in compliance with HUD requirements. The Municipality stated that any cases that did not comply would be referred to the legal division for corresponding action.

We reviewed the additional documentation provided and determined it did not properly support the principal residency requirement. For example, the mailing address for some of the utility bills provided as support was different from the address of the HOME assisted property without any explanation. Since the information was conflicting, we did not revise the audit report or recommendations.

Comment 6 The Municipality claimed that the requirements of the National Defense Authorization Act of 1991 did not apply to three projects and that three projects were in compliance with such requirements. The Municipality indicated that HUD's system uses a First-In First-Out (FIFO) method for committing and drawing funds and based on this method, it had complied with the timely disbursement of funds. It also evaluated HOME expiring funds reports and determined none of the projects reviewed had expiring balances listed in the report.

Contrary to the Municipality statement, the FIFO method and the HOME expiring reports have no bearing on the eligibility of commitments and expenditures. The compliance with the requirements of the National Defense Authorization Act is not based on the year when the HOME project's funds were issued. The determining factor is whether the projects had funds committed from grants dated 2002 and after. All projects under recommendations 1A and 1B included such commitments. The Municipality did not provide additional support regarding the eligibility of costs in recommendations 1A and 1B. On a case by case basis, HUD should determine whether the closure and deobligation of funds associated with recommendations 1A and 1B would generate any shortfalls related to the statutory requirements of the National Defense Authorization Act of 1991 and/or Title II of the Cranston-Gonzalez National Affordable Housing Act, and recapture the funds as appropriate.

Comment 7 The Municipality stated that it had revised its monitoring procedures to review the affordability and principal residency requirements for homeownership activities.

OIG did not evaluate the new procedures. HUD must ensure the adequacy and proper implementation of the new procedures. OIG will evaluate the adequacy of procedures with HUD during the audit resolution process.

Comment 8 The Municipality provided additional documentation related to the costs questioned in recommendation 2A.

We reviewed the additional documentation and determined it was sufficient to support the eligibility of \$672,817. As a result, we revised the finding and renumbered this recommendation as 2B.

Comment 9 The Municipality stated that, based on Notice CPD 06-01, it charged wages of two municipal employees as project related soft costs that were eligible. It contended that no time allocation was necessary because the staff was only performing duties related to the HOME program, and because the notice did not require it.

The HOME program allows disbursements for eligible project costs, including staff and overhead costs directly related to carrying out the project, such as services related to assisting potential owners, tenants, and home buyers. In addition, all costs to be allowable must be reasonable and supported with records that enable HUD to determine its compliance with all program requirements. The Municipality did not provide additional documentation to show the eligibility, propriety, the basis used, and reasonableness of wages charged as activity delivery costs. Therefore, we did not change the audit report and the recommendations.

Comment 10 The Municipality claimed that its accounting records are accurate, current, and complete. It believed that auditors may have used revised vouchers in its calculation of HOME program disbursements. The Municipality stated that it will perform a review of all drawdowns made between July 1, 2011, and October 31, 2013. It will provide HUD with the results of such review by October 31, 2014.

We do not concur with the Municipality's claim that the accounting records were accurate, current, and complete. As discussed in the report, the records did not reflect disbursements by grant activity and funding type and did not properly account for capital assets. In addition, the general ledger accounts did not reflect the correct balance and did not provide individual accounts for the recording of receipts associated with program income, recaptured funds, and repayments. The Municipality did not provide additional documentation to demonstrate the propriety of the disbursements or that its accounting records were accurate, current, and complete.

Comment 11 The Municipality stated that it reimbursed the \$317,701 and that it provided evidence demonstrating it complied with HOME program requirements.

We reviewed the documentation provided and the Municipality did support the return of \$261,599 to its treasury account as required by HUD. The Municipality did not provide evidence that the remaining \$56,102 was returned as claimed. As a result, we revised the finding and recommendation 2C accordingly. Based on the changes made, the previous Recommendation 2C was moved to

Recommendation 2D, and vice versa.

Comment 12 The Municipality indicated that HUD does not require that reimbursed funds be returned to the treasury account and requested the elimination of recommendation 2C.

Contrary to the Municipality's claim, any unexpended drawdowns must be returned. HUD regulations at 24 CFR 92.502(c)(2) state that HOME funds drawn down from a participating jurisdiction's treasury account must be expended for eligible costs within 15 days and any unexpended drawdowns must be returned to HUD. Memorandum entitled "Repayment of HOME Funds Used for Ineligible Activities or Ineligible Costs and Return of HOME Funds to the Treasury Account", dated April 5, 2011, further clarifies that funds drawn down from the HOME Investment Trust Fund Treasury account in advance of need or in excess of need be returned to the Treasury account. Once HOME funds drawn down are returned, the participating jurisdiction must revise applicable vouchers to accurately represent actual eligible HOME disbursement for activities in HUD's system. As a result, the recommendation was not eliminated.

Comment 13 The Municipality stated that OIG's statement that \$11,000 in HOME funds was used to reimburse a 2010 HUD monitoring finding was incorrect and unsupported. It claimed that local funds were transferred on March 30, 2012, to the HOME account and that these funds were used to pay the monitoring finding. Regarding the \$51,204 in ineligible disbursements, the Municipality stated that it will set aside in the next year's local budget the funds and reimburse the HOME program.

The documentation submitted by the Municipality did not support their claim that the reimbursement was made with local funds. In addition, the amount transferred did not agree with the \$11,000 questioned. The Municipality did not provide any additional documentation explaining the inconsistencies. As a result we did not change the audit finding and recommendations. HUD should require the immediate reimbursement of the \$62,204 improperly disbursed.

Comment 14 The Municipality stated that it implemented a new financial management system and that it developed and implemented procedures to ensure funds are disbursed in a timely manner. It also stated that it had developed procedures to facilitate the management of program income and that all program income will be deposited in a separate bank account.

HUD must ensure the Municipality properly monitors the accuracy of all information reported in HUD's information system and correct any inaccuracies. OIG will evaluate the adequacy of procedures with HUD during the audit resolution process.

Appendix C

LIST OF ACTIVITIES NOT MEETING PRINCIPAL RESIDENCY REQUIREMENT

Activity number	Housing project	Unit number	Amount	Description
288	San Ciprian II	107	\$24,704	Unit was repossessed by bank.
288	San Ciprian II	109	\$21,704	Municipality could not verify occupancy.
288	San Ciprian II	112	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	114	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	203	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	210	\$21,704	Municipality could not verify occupancy.
288	San Ciprian II	211	\$21,704	Municipality could not verify occupancy.
288	San Ciprian II	214	\$21,704	Municipality could not verify occupancy.
288	San Ciprian II	215	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	305	\$31,704	Municipality could not verify occupancy.
288	San Ciprian II	310	\$21,704	Municipality could not verify occupancy.
288	San Ciprian II	313	\$31,704	Municipality could not verify occupancy.
288	San Ciprian II	314	\$31,704	Municipality could not verify occupancy.
288	San Ciprian II	315	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	316	\$16,704	Municipality could not verify occupancy.
288	San Ciprian II	317	\$24,704	Municipality could not verify occupancy.
288	San Ciprian III	111	\$28,907	Participant did not live in the unit.
288	San Ciprian III	304	\$28,907	Participant did not live in the unit.
288	San Ciprian III	309	\$28,907	Unit was vacant.
288	San Ciprian III	314	\$28,907	Unit was leased.
288	San Ciprian III	318	\$39,407	Unit was leased.
351	Balcones de Carolina III	A3-301	\$23,290	Participant did not live in the unit.
351	Balcones de Carolina III	B3-402	\$10,571	Municipality could not verify occupancy.
351	Balcones de Carolina III	C3-402	\$10,571	Participant did not live in the unit.
351	Balcones de Carolina III	D3-101	\$10,571	Participant did not live in the unit.
351	Balcones de Carolina III	D3-201	\$9,298	Municipality could not verify occupancy.
351	Balcones de Carolina III	D3-401	\$9,298	Participant did not live in the unit.
351	Balcones de Carolina III	E3-401	\$10,571	Unit was vacant.
351	Balcones de Carolina III	F3-302	\$10,571	Participant did not live in the unit.
351	Balcones de Carolina III	I3-302	\$9,298	Participant did not live in the unit.
351	Balcones de Carolina III	I3-401	\$10,571	Participant did not live in the unit.
351	Balcones de Carolina III	K3-302	\$10,399	Participant did not live in the unit.
351	Balcones de Carolina III	03-202	\$9,298	Participant did not live in the unit.
351	Balcones de Carolina III	03-301	\$23,290	Participant did not live in the unit.
351	Balcones de Carolina III	03-302	\$9,298	Participant did not live in the unit.
Total			<u>\$675,194</u>	