



**Windridge Apartments  
Wichita, KS**

**Section 221(d)(4) Multifamily Insurance Program**



U.S. DEPARTMENT OF  
HOUSING AND URBAN DEVELOPMENT  
OFFICE OF INSPECTOR GENERAL

Issue Date: November 7, 2013

Audit Report Number: 2014-KC-1001

TO: Joseph D. Pennel, Acting Director, Kansas City Office of Multifamily Housing,  
6AHMLAS

//signed//

FROM: Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

SUBJECT: Windridge Apartments Did Not Administer Its Program in Accordance With  
HUD Rules and Regulations and Its Own Policies and Procedures

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Windridge Apartments.

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 913-551-5870.



November 7, 2013

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## **Windridge Apartments Did Not Administer Its Program in Accordance With HUD Rules and Regulations and Its Own Policies and Procedures**

# **Highlights**

**Audit Report 2014-KC-1001**

### **What We Audited and Why**

We selected Windridge Apartments in Wichita, KS, for audit based on a referral from the Region 7 Office of Multifamily Housing due to high tenant receivables and excessive travel expenses. Our audit objectives were to determine whether Windridge Apartment Associates, L.P., (1) followed U.S. Department of Housing and Urban Development (HUD) rules and regulations when it procured products and services, (2) followed HUD rules and regulations and its own policies and procedures for rent collection, and (3) followed HUD rules and regulations when charging travel expenses to the operating account.

### **What We Recommend**

We recommend that HUD require the property to provide cost justification for \$200,362 spent on goods or services and have the management agent reimburse the property for \$39,466 in ineligible travel expenses.

### **What We Found**

The property (1) did not obtain three written cost estimates for goods or services expected to exceed \$10,000, (2) did not provide proper notice and start eviction procedures for nonpayment of rent, and (3) paid more than \$39,000 in travel expenses for individuals not employed by the property.

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## BACKGROUND AND OBJECTIVES

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Windridge Apartments is located at 2502 Wildwood Lane, Wichita, KS. The property is a 136-unit housing project insured under the U.S. Department of Housing and Urban Development's (HUD) section 221(d)(4) of the National Housing Act. HUD regulates the property's rent charges and operating methods.

HUD's control over the property is exercised by a regulatory agreement, form HUD-92466, signed on September 13, 2007. The agreement outlines terms and conditions for the HUD-insured mortgage, such as what expenses can be paid with project funds.

The property is owned by Windridge Apartments Associates, L.P., and the general partner is Windridge-Michaels, LLC. The property's management agent, Interstate Realty Management Company, is an identity-of-interest management agent. A majority of the property's day-to-day activities are managed at the property, while the bulk of the financial operations are managed at the management agent's home office in Marlton, NJ.

The property receives a material portion of its revenue under a Federal Section 8 rent subsidy program for 133 of its 136 units. This program provides for direct rent subsidy payments to the property on behalf of certain tenants who qualify under the program's rules. Between January 1, 2010, and March 31, 2013, the Property received more than \$2.9 million in housing assistance payments.

Our audit objectives were to determine whether Windridge Apartment Associates, L.P.,

- (1) Followed HUD rules and regulations when it procured products and services for the property,
- (2) Followed HUD rules and regulations and its own policies and procedures for rent collection, and
- (3) Followed HUD rules and regulations when charging travel expenses to the operating account for travel to the property in preparation for a management review.

## RESULTS OF AUDIT

### Finding 1: The Property Did Not Obtain Three Written Cost Estimates for Goods or Services Expected To Exceed \$10,000

The property did not obtain written cost estimates from at least three contractors for goods or services expected to exceed \$10,000. This condition occurred because the property did not have adequate procurement policies and procedures. As a result, it could not ensure that more than \$200,000 spent on goods or services were reasonable.

#### The Property Did Not Obtain Written Cost Estimates

The property did not obtain written cost estimates from at least three contractors for goods or services exceeding \$10,000. It had one contract for trash collection and waste management, and it used a sourcing company to negotiate this contract. However, neither the property nor the sourcing company obtained written cost estimates from at least three contractors for this service. In 2011 and 2012, the property spent \$32,511 on waste management.

Further, although the property had only the one contract in place, it received ongoing supplies or services for grounds maintenance, wall repair and painting, carpet and carpet installation, security and protection services, and audit services. The amount paid for each of these supplies or services exceeded \$10,000 for calendar years 2011 and 2012; however, the property did not receive written cost estimates from at least three contractors. In 2011 and 2012, it spent \$167,851 for ongoing supplies and services. The property's expenses are detailed in the table below.

Goods or services	2011	2012	Total
Audit services	\$11,250	\$12,350	\$23,600
Grounds	10,350	*	10,350
Trash collection & waste management	14,496	18,015	32,511
Security & protection services	**	14,352	14,352
Wall repair & painting	42,812	26,933	69,745
Carpet & carpet installation	13,308	36,496	49,804
<b>Total</b>	<b>\$92,216</b>	<b>\$108,146</b>	<b>\$200,362</b>

\* Funds spent in 2012 did not exceed \$10,000 threshold

\*\* Funds spent in 2011 did not exceed \$10,000 threshold

In total, the property spent more than \$200,000 for goods or services without obtaining at least three written cost estimates. According to HUD Handbook 4381.5, paragraph 6.50, when contracting for goods or services, the property was expected to solicit written cost estimates for any contract, ongoing supply, or service that was expected to exceed \$10,000 per year

This condition occurred because the property did not have adequate procurement policies and procedures. Its contract policy consisted of guidelines for contracts and did not provide guidance for establishing cost reasonableness for contracts and ongoing supplies or services. As a result, the property could not ensure that more than \$200,000 spent on goods or services were reasonable.

## Recommendations

We recommend that the Acting Director of HUD's Kansas City Office of Multifamily Housing require the property to

- 1A. Provide cost justification for the \$200,362 spent on goods or services in fiscal years 2011 and 2012 and any goods or services expected to exceed \$10,000 in fiscal year 2013 by obtaining written cost estimates from at least three contractors or reimburse the unsupported amount to the property's operating account from non-project funds.
- 1B. Develop and implement procurement policies and procedures to ensure compliance with HUD regulations, including Handbook 4381.5, paragraph 6.50.

## RESULTS OF AUDIT

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### Finding 2: The Property Did Not Provide Proper Notice and Start Eviction Procedures for Nonpayment of Rent

The property did not provide proper notice and start eviction procedures for nonpayment of rent in accordance with its policy. This condition occurred because the property manager disregarded the rent collection policy. As a result, the property lacked funds in its operating account to pay other property expenses.

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#### **The Property Did Not Provide Proper Notice and Start Eviction Procedures**

The property did not provide notice and start eviction procedures for nonpayment of rent in accordance with its policy. The property's rent collection policy required it to provide tenants with an initial notice of late rent, allowing the tenant 10 days to meet with the property manager and discuss the pending lease termination for nonpayment of rent. According to the property's policy, the property manager should serve a second notice 7 days from the initial notice, allowing the tenant 3 days to pay rent or vacate the property. If the tenant still had not paid the rent, the property should begin eviction procedures 3 days following the second notice.

This condition occurred because the property manager disregarded the rent collection policy. The property manager served tenants with a 3-day notice to pay or vacate for nonpayment of rent without mentioning that the tenant had 10 days to discuss the termination with property staff. Additionally, the tenants were not served with a second notice if rent remained unpaid after 7 days, in accordance with its policy. Instead, the property waited until the tenant did not pay for a second month before serving a second notice and starting eviction procedures.

As a result of not collecting rent and not starting eviction procedures in accordance with its policy, the property lacked funds in its operating account to pay other property expenses. As of December 31, 2012, the property owed its management agent more than \$298,000 at a time when the property had \$46,136 in tenants' accounts receivable, including \$18,268 due to nonpayment of rent.



## Recommendations

We recommend that the Acting Director of HUD's Kansas City Office of Multifamily Housing

- 2A. Require the property to implement its existing rent collection policy.
- 2B. Perform additional monitoring to ensure the rent collection policy is properly implemented by the property.

## RESULTS OF AUDIT

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### Finding 3: The Property Paid for Travel Expenses for Individuals Not Employed by the Property

The property paid travel expenses for individuals not employed by the property. This condition occurred because the property did not have a travel expense policy. As a result, it did not have over \$39,000 in its operating account to pay other property expenses.

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#### The Property Paid for Travel Expenses for Nonemployees

The property paid for travel expenses for individuals who were not front line employees of the property. In discussions with property staff, we learned that the individuals traveled to the property to prepare for monitoring reviews and physical inspections. Further, after receiving an unsatisfactory rating during a management review in 2011, the property had these individuals travel to the property to help clean up the physical property and tenant files. These files and the physical property should be properly maintained by front line staff. Preparation before and correction of deficiencies found after a review or inspection should not be necessary if they are adequately performing their front line duties. If their performance is not adequate, this is a management problem to be dealt with at the management agent level and at a cost to the management agent. The table below outlines the property's travel expenses, and the table in Appendix C includes a more detailed breakdown.

Year	Travel Expenses
2011	\$37,560
2013	1,905
<b>Total</b>	<b>\$39,465</b>

Note: In 2012, the property did not incur any travel expenses for nonemployees.

This condition occurred because the property did not have a travel expense policy that ensured only travel costs related to the project were paid. The property's management agent charged the travel expenses to the property because it incorrectly classified the travel as an allowable front-line travel expense, such as meeting with contractors or making bank deposits. However, according to HUD Handbook 4381.5, paragraph 6.39(b)(1), costs for designing procedures/systems to keep the project running smoothly and in conformity with HUD requirements should be paid out of management fee funds. Furthermore, paragraph 6.39(b)(5) states fees associated with monitoring projects by visiting the project should be

taken from the management fee and not charged to the operating account. Therefore, the property's management agent should have paid for the travel expenses and not the property.

As a result of the improper payment, the property did not have these funds available to pay other property expenses. In 2011 and 2013, the property spent more than \$39,000 on travel expenses for individuals not employed by the property.

## Recommendations

We recommend that the Acting Director of HUD's Kansas City Office of Multifamily Housing require

- 3A. The management agent to reimburse the property for the \$39,465 in ineligible travel expenses.
- 3B. The property to create and implement a travel expense policy to ensure compliance with HUD Handbook 4381.5.

## SCOPE AND METHODOLOGY

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Our review generally covered the period January 1, 2011, through March 31, 2013. We performed onsite work from April 29 through June 21, 2013, at Windridge Apartments, located at 2502 Wildwood Lane, Wichita, KS.

To accomplish our objectives, we

- Reviewed applicable Federal regulations and HUD handbooks, as well as the property's tenant selection plan, rent collection policy, and other internal policies and procedures;
- Reviewed the property's audited financial statements;
- Reviewed the property's general ledger and monthly accounting reports;
- Reviewed support for the property's travel expenses for January 1, 2011, through March 31, 2013; and
- Interviewed property and HUD Kansas City Office of Multifamily Housing staff.

We reviewed a sample of 40 of 216 tenant files (18.5 percent). We selected 2 of the 40 tenants because they had the largest credit balances as of December 31, 2012, and we selected another 35 of the 40 due to the tenants' owing the highest amount of rent and damages to the property. Additionally, we randomly selected one tenant who was written off as uncollectible in 2012, and we randomly selected the last two tenants from the 2012 tenants' accounts receivable listing. As of December 31, 2012, the tenants selected collectively owed \$14,823 in unpaid rent and \$23,687 in damages, totaling \$38,510 in tenants' accounts receivable. As of December 31, 2012, the property had \$46,136 in tenants' accounts receivable, but before that date, the property wrote off more than \$35,000 in 2012 and \$49,000 in 2011.

We also reviewed a sample of 194 invoices totaling \$76,615. We randomly selected 29 of the 194 invoices from the property's general ledger after reviewing the ledger for expenses exceeding \$10,000 annually. The other 165 invoices represented 100 percent of invoices for 2011 and 2012 for three vendors that performed heating and air conditioning repair for the property. The population from which we selected our sample consisted of 1,072 invoices totaling \$380,329. We sampled more than 20 percent of the total dollar amount of the population.

We relied, in part, on accounting data provided by the property. Although we did not perform a detailed assessment of the reliability of the data, we determined that the computer-processed data were sufficiently reliable to be used in meeting our objectives because the data in the sampled items were corroborated by documentary evidence that the property supplied for the sampled vendors.

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

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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.

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## Relevant Internal Controls

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

- Controls over procurement, rent collection, travel, and damage assessment.

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 property did not have adequate procurement policies and procedures to ensure that HUD funds were expended in compliance with HUD rules and regulations (see finding 1).
- The property did not have adequate travel expense policy to prevent travel for nonemployees from being charged to the property's operating account (see finding 3).

## **Separate Communication of Minor Deficiencies**

We reported minor deficiencies to the auditee in a separate management memorandum.

## APPENDIXES

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### Appendix A

#### SCHEDULE OF QUESTIONED COSTS

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Recommendation number	Ineligible 1/	Unsupported 2/
1A		\$200,362
3A	\$39,465	

- 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.




# Appendix B

## AUDITEE COMMENTS AND OIG'S EVALUATION

### Ref to OIG Evaluation

### Auditee Comments

#### Comment 1

	<b>INTERSTATE REALTY MANAGEMENT CO.</b>
ATLANTIC CITY NJ CHESTER PA CHICAGO IL DETROIT MI FT WORTH TX IRVINE CA JACKSON MS JACKSONVILLE FL KANSAS CITY MO LODI CA MARLTON NJ NEW ORLEANS LA PHILADELPHIA PA PITTSBURGH PA TAMAQUA PA TRENTON NJ TULSA OK TUPELO MS	<p><b>VIA EMAIL AND OVERNIGHT MAIL</b></p> <p>October 4, 2013</p> <p>Mr. Ronald J. Hosking Regional Inspector General for Audit U.S. Department of Housing and Urban Development Office of Inspector General - Office of Audit Region 7 400 State Avenue – Suite 501 Kansas City, KS 66101</p> <p>Dear Mr. Hosking:</p> <p>This letter is in response to the Audit Report discussion draft (the “Draft Report”) concerning Windridge Apartments (“Windridge” or the “Property”) issued by the U.S. Department of Housing and Urban Development (“HUD” or the “Department”) Office of Inspector General – Office of Audit Region 7 (the “IG”) on September 12, 2013, and which was the subject of an exit conference held on September 24, 2013 (the “Exit Conference”). Having been provided an extension to October 4, 2013, this response is timely.</p>
Corporate Office	<p style="text-align: center;"><b>Introduction</b></p> <p>As you know, Windridge is a 136-unit apartment complex located in Wichita, Kansas. The Property is owned by Windridge Apartments Associates, L.P., and its management agent is Interstate Realty Management Company (“IRM”), an identity-of-interest management agent. The Property is subject to HUD oversight given that its financing is insured under Section 221(d)(4) of the National Housing Act, and that nearly all of its units receive Section 8 subsidy.</p> <p>The responses set forth below reflect IRM’s understanding of changes to the Draft Report that the IG agreed to following the Exit Conference. It is also IRM’s understanding that these changes will be included in the final Audit Report that will be issued after incorporation and consideration of the responses provided in this letter. The changes include deleting one finding altogether and instead including it in a separate management letter of minor deficiencies, as well as revising the wording of the three remaining findings, including but not limited to changes made to more accurately reflect the status of certain of the Property’s policies and procedures.</p>
	
	



**Ref to OIG Evaluation**

**Auditee Comments**

**Comment 1**

**Discussion**

**Finding 1: The Property Did Not Obtain Three Written Cost Estimates for Goods or Services Expected to Exceed \$10,000**

With regard to six categories of goods or services, the Draft Report asserts that Windridge did not obtain written cost estimates from at least three contractors as required by the applicable HUD guidance for ongoing supplies or services expected to exceed \$10,000 per year (see HUD Handbook 4381.5 Section 6.50 (the "HUD Guidance")). According to the Draft Report, this occurred because Windridge did not have adequate procurement policies and procedures in place, and as a result, the Property could not ensure that the expenditures at issue were reasonable.

As discussed below, in certain instances the Draft Report failed to take into account that Windridge was faced with applying HUD Guidance that is tied to a vague notion of "expected" costs for which there is no clear standard. In other instances also discussed below, the Draft Report failed to take into account the particular facts and circumstances of the expense categories Windridge addressed, including current and real world business models and practices not contemplated by the decades old HUD Guidance.

We note that the Draft Report includes a recommendation that following issuance of the final Audit Report, the HUD Kansas City Regional Office's Multifamily Hub ("KC Multifamily") should require Windridge to provide cost justification for the expenses incurred. Although it would have been preferable for Windridge to have had the opportunity to provide the information during the audit process, thereby obviating the finding made in the Draft Report altogether, if Windridge is requested to do so by KC Multifamily, we are confident that such information will be provided to KC Multifamily's satisfaction and that the finding will be fully resolved.

*Audit Services*

As set forth in the Draft Report, Windridge incurred audit service expenses in the amount of \$11,250 in 2011 and \$12,350 in 2012. As explained during the IG audit process, these audit services were performed by a highly respected professional services firm with both operations throughout the United States and abroad and a high level of experience with HUD audit requirements and related deadlines. The amounts paid were flat fees for audit and tax return services that reflected a discount from the audit firm's "rack rates" because of the large number of audits it undertook for IRM managed properties over multiple years. As such, the arrangement reflected a modern-day, business-oriented approach that was advantageous for Windridge from both cost and work product quality perspectives. Because the audit firm was in a position to leverage its keen understanding of Windridge's financial operations which as stated in the Draft Report itself, was largely managed at IRM's home office, as well as economies of scale, it was able to provide a high-quality product at a reasonable price delivered on time.

As we explained during the audit process with regard to the price and quality factors, IRM made an ongoing assessment of the audit firm's performance and fees compared with other firms, including the fees paid by IRM fee managed (i.e., non-identity of interest) properties to such other firms. IRM data indicates that the Windridge audit fee is in the middle range of fees charged in those circumstances. IRM has had direct experience with firms who may charge a lower rate but are unable to provide the same quality of audit or meet the submission deadlines. As such, Windridge made a common sense, current business environment driven determination that as long as the audit firm's fees were reasonable and the quality of its work remained high, the firm could permissibly provide audit services for Windridge.

*Grounds*

As set forth in the Draft Report, Windridge incurred grounds expenses in the amount of \$10,350 in 2011 and under the \$10,000 threshold in 2012. As such, the Draft Report takes issue with the grounds expenses for 2011.

In 2011, the grounds expenses exceeded \$10,000 due to expenses incurred to address damage caused by an unusually severe storm, including \$1,080 for tree removal and fence repair. Windridge had no reason to expect that the grounds expenses for 2011 would exceed \$10,000. To the extent the grounds expenses exceeded \$10,000 in 2011, crossing the threshold was due to unforeseeable circumstances and therefore was unexpected. As acknowledged in the Draft Report, grounds expenses for 2012 did not exceed the \$10,000 threshold, further demonstrating that Windridge not anticipating that 2011 grounds expenses would exceed the \$10,000 threshold was reasonable.

*Trash Collection and Waste Management*

As set forth in the Draft Report, Windridge incurred trash collection and waste management expenses in the amount of \$14,496 for 2011 and \$18,015 for 2012. As we explained during the audit process, the provider of trash and recycling services for Windridge was selected with the assistance of a solid-waste and recycling service purchasing firm that assists multi-family housing management with obtaining such services. We required that the firm obtain, and the firm agreed to obtain, at least three bids prior to its recommending the award of a contract for the trash and recycling services. However, for the contract that included 2011 and 2012, because the firm had determined that there were only two qualified service providers in the area, and because the pricing offered by the provider selected for Windridge continued to be lower than what had previously been quoted by the other qualified provider, the firm recommended that Windridge continue to contract with the lower-priced provider, which Windridge did.

Although we continue to believe that this explanation provides sufficient grounds to warrant that the expenses incurred for trash collection and waste management not be included as part of the audit finding, we have advised the firm that if they are still being used when the contract with the current service provider for Windridge expires, it will need to confirm the number of qualified service providers and, if there are fewer than

## Ref to OIG Evaluation

## Auditee Comments

three, it will need to receive written bids from them all, and if there are three or more, it will need to get written bids from at least three.

### *Security and Protection Services*

The Draft Report provides that Windridge incurred expenses for security and protection services in an amount less than the \$10,000 threshold for 2011, and for 2012, the amount increased to \$14,352. As such, the Draft Report takes issue with the security and protection services expenses for 2012.

In 2012 the security expenses rose from the previous year's amount to \$14,352, primarily due to costs incurred during the course of the year to address increasingly problematic levels of serious crime at the Property and in the surrounding community. We note that the local HUD office was keenly aware of this increase in crime, and being good stewards, Windridge increased security which not only served the best interests of the Property's residents, but also HUD and the local police department.

The increase in expenses to over the \$10,000 threshold as determined by the IG was not foreseeable as required by the HUD Guidance in order to trigger the requirement that three written bids be obtained. Moreover, as further demonstration of the fact that Windridge did not act with disregard of the HUD Guidance and its foundational principle that projects expenses must be reasonable, although not required under the HUD Guidance, in late 2011 and early 2012, having become very concerned about the crime issue, Windridge conscientiously inquired into the security and protection services available in the area to best address the situation. In doing so, Windridge obtained bids from two private companies in the area that at the time could provide the services (one of which was the incumbent provider), and reached out to the local police department to determine if off-duty officers were available to provide the services, which they were not. Based on that information, Windridge determined to continue to retain the services of the incumbent security and protection services provider.

### *Wall Repair and Painting*

As set forth in the Draft Report, Windridge incurred expenses for wall repair and painting for 2011 in the amount of \$42,812 and for 2012 in the amount of \$26,933. As we explained during the audit process, most of the labor associated with wall repair and painting was performed by one service company, and the supplies related thereto were obtained through Buyers Access.

Regarding the labor costs, because the nature, scope and frequency of such repairs is inherently unpredictable and largely piecemeal on an as-needed basis, a reasonable interpretation of the HUD Guidance applied by Windridge was that getting three bids for the labor needed each time a wall repair and painting job arose was not required. Rather, having knowledge of pricing for similar work in the area, including previous work done at Windridge, the Property determined to contract with service providers who offered reasonable pricing and that performed quality work.

**Ref to OIG Evaluation**

**Auditee Comments**

A similar analysis should apply to Windridge's purchase of wall repair and painting supplies. Buyers Access is well-known and respected group purchasing program that provides volume discounts to the apartment industry through pre-negotiated pricing. To date, there are over 600,000 units enrolled in the program nationwide. As Windridge explained during the audit process, it is confident that the prices charged for supplies purchased through the Buyers Access program were competitive. Buyers Access did not dictate that Windridge use its suppliers, but because of the cost and operational efficiencies of its business model, Buyers Access was able to negotiate competitive prices. Additionally, Buyers Access pricing remained firm for its calendar year which runs from May 1<sup>st</sup> to April 30<sup>th</sup> for most suppliers since during that year, the prices for standard products in its catalogs (like carpeting and paint) cannot be raised for its members. As a result, although the prices of many suppliers increased throughout the year, Windridge was insulated from those price increases. Finally, if a product was put on sale by a supplier and the sales price was lower than the regular Buyers Access price, Windridge received the best price through Buyers Access. Due to Buyers Access' ability to negotiate favorable prices, Windridge's insulation from dramatic price increases, and the opportunity to receive the best sales price, Windridge was confident that the pricing for the supplies was competitive.

*Carpet and Carpet Installation*

As set forth in the Draft Report, Windridge incurred expenses for carpet and carpet installation for 2011 in the amount of \$13,308 and for 2012 in the amount of \$36,496. As we explained during the audit process, the supplies and labor related to these expenses were obtained through Buyers Access whose benefits are outlined above.

Finding 2: The Property Did Not Provide Proper Notice and Start Eviction Procedures for Nonpayment of Rent

According to the Draft Report, Windridge disregarded its rent collection policy and therefore did not provide proper notice and start eviction procedures for nonpayment of rent in accordance with that policy. The Draft Report further alleges that because of this, Windridge lacked funds in its operating account to pay other Property expenses.

As Windridge explained during the audit process, the document that the auditors relied upon in making this finding and that was reprinted in Appendix D of the Draft Report is not the Windridge rent collection policy. Rather, it was a document dating back to at least April 2010 that had inadvertently been left posted in the Property's office. Windridge is confident that since at least April 2010 when the Property was added to the portfolio of the current IRM District Property Manager for Windridge, the posting did not and currently does not reflect Windridge's actual policies and practices and has not been applied at the Property.

The rent collection policy that was actually being applied at Windridge since at least April 2010 was and continues to be the policy set forth in Windridge's Community Policies. This policy was also posted in the office, below where the document focused on

**Comment 2**

**Ref to OIG Evaluation**

**Auditee Comments**

**Comment 3**

by the IG auditors had been posted. As required by HUD, the Community Policies document is listed in the HUD model lease used at Windridge as an attachment to the lease (referred to as the House Rules in the lease), and upon receipt of the Community Policies, the tenant signs another document stating that they received a copy of the Community Policies. .

Moreover, if the Draft Report had included an assessment of the actual Windridge rent collection policy and how that policy was applied in conjunction with the Property's lease termination procedures for failure to pay rent, an adverse finding in the Draft Report would not have been indicated. As advised by the Property's local landlord-tenant counsel, Kansas law requires that tenants receive a 3 day notice to quit before the landlord can proceed with eviction for nonpayment of rent. As such, this type of notice is provided at Windridge. Windridge also applies the provision in HUD's model lease which is used at the Property and which requires that the tenant be provided with 10 days to discuss the proposed termination of tenancy with the landlord. This 10 day notice is provided due to the length of time it takes to get the eviction on the local court's docket as well as the extra time Windridge provides its tenants out of compassion and decency to become current on their overdue rent. Thus, in practice all tenants are given well over the 10 day notice that is required by the HUD model lease. As such, when Windridge's Contract Administrator has reviewed the Property's rent collection policy and related practices during its MORs of the Property, it has not raised issues in that regard. Finally, even had there been an issue with the Windridge's rent collection policy as described in the Draft Report, in no way would it have resulted in Windridge lacking funds in its operating account to pay other Property expenses. Contrary to what is thereby implied in the Draft Report, Windridge's has no history of failing to pay its expenses on a timely basis. Rather, to the extent needed, IRM, as a good HUD partner, has deferred its management fee so that the Property would not be in the position of having to do so.

Finding 3: The Property Paid for Travel Expenses for Individuals Not Employed by the Property

According to the Draft Report, because Windridge did not have an adequate travel expense policy it inappropriately paid \$39,465 in such expenses for persons not employed by Windridge. The Draft Report further asserts that as a result, the \$39,465 was not available to pay other Property expenses.

**Comment 3**

Although we disagree with certain aspects of the Draft Report's analysis which form the basis of this finding, for the purpose of reaching closure on the audit process, IRM has determined that as to the specific circumstances described in the Draft Report which led to Windridge paying the travel expenses at issue, it will agree to reimburse the property for the \$39,465 at issue. However, we note again that contrary to what is implied in the Draft Report, Windridge's treatment of the travel expenses at issue (or any other expenses for that matter) did not mean that it failed to pay its expenses on a timely basis. Rather, to the extent needed, IRM deferred its management fee so that the Property could meet its expenses.

**Ref to OIG Evaluation**

**Auditee Comments**

**Conclusion**

IRM appreciates the professionalism and courteousness with which the IG conducted its audit of Windridge and looks forward to working with KC Multifamily to present information needed to close-out any finding not resolved by the IG in its final Audit Report. Should you have any questions of need any additional information; I can be reached at [REDACTED]

Sincerely,



Mark Morgan, CPM  
President  
Interstate Management Company



## OIG Evaluation of Auditee Comments

- Comment 1** The property did not provide documentation to support they obtained cost estimates from additional contractors, nor were they able to provide support that the sourcing company had obtained cost estimates from other vendors. Further, the property did not take steps to ensure that the prices provided by Buyers Access were reasonable by obtaining cost estimates from at least three contractors.
- Comment 2** The rent collection procedures provided by the property and posted in the property's office were the only procedures that stated the steps the property would take to collect the rent. Additionally, the property's rent agreement states that all termination notices must specify the date the agreement will be terminated and advise the tenant that he/she has 10 days to discuss the proposed termination of tenancy with the landlord. The property served tenants with a three-day notice to pay or evict, and did not follow through with evictions in accordance with the notice when tenants failed to pay rent.
- Comment 3** The fees owed to the management agent are considered property expenses and should be paid timely. As of December 31, 2012, the property's accounts payable balance included \$298,756 payable to its management agent for management fees, bookkeeping fees, and payroll and related expenses. This amount increased more than \$63,000 from 2011.

## Appendix C

### INELIGIBLE AND UNSUPPORTED COSTS DETAIL

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#### Finding 3 – Travel expenses

Employee	2011	2013
1	\$3,223	\$ 0
2	7,577	0
3	300	0
4	1,722	0
5	427	0
6	1,962	0
7	4,378	0
8	2,507	942
9	1,781	963
10	2,076	0
11	2,836	0
12	468	0
13	559	0
14	684	0
15	876	0
16	225	0
17	178	0
18	492	0
19	210	0
20	5,079	0
<b>Total</b>	<b>\$37,560</b>	<b>\$1,905</b>

Note: The property did not incur any travel expenses for nonemployees in 2012.



## Appendix D

### CRITERIA

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#### Form HUD-9839-B – Project Owner’s/Management Agent Certification

3. We agree to:
  - a. Comply with this project’s Regulatory Agreement, Mortgage & Mortgage Note, and any Subsidy Contract or Workout/Modification Agreement.
  - b. Comply with HUD handbooks, notices or other policy directives that relate to the management of the project.
4. The Agent agrees to:
  - a. Ensure that **all** expenses of the project are reasonable and necessary.
  - b. Exert reasonable effort to maximize project income and take advantage of discounts, rebates and similar money-saving techniques.
  - c. Obtain contracts, materials, supplies and services, including the preparation of the annual audit, on terms most advantageous to the project.
  - d. Credit the project with **all** discounts, rebates or commissions (including any sales or property tax relief granted by the State and local government) received.
  - e. Obtain the necessary verbal or written cost estimates and document the reasons for accepting other than the lowest bid.
  - f. Maintain copies of such documentation and make such documentation available for your inspection during normal business hours.
  - g. Invest project funds that HUD policies require to be invested and take reasonable effort to invest other project funds unless the owner specifically directs the Agent not to invest those other funds

#### HUD Handbook 4381.5, REV 2 – The Management Agent Handbook, Chapter 6

##### 6.39 Management Costs Paid from the Management Fee

- a. Expenses for services that are not front-line activities must be paid out of management fee funds, except for centralized accounting and computer services.
- b. Salaries, fringe benefits, office expenses, fees, and contract costs for the following activities must be paid out of management fee funds. These costs include:
  - (1) Designing procedures/systems to keep the project running smoothly and in conformity with HUD requirements
  - (2) Preparing budgets required by the owner or HUD, exclusive of rent increase requests and MIO (Management Improvement and Operating) Plans.
  - (3) Recruiting, hiring, and supervising project personnel.
  - (4) Training for project personnel that exceeds the line item budget for training expenses.
  - (5) Monitoring project operations by visiting the project or analyzing project performance reports.
  - (6) Analyzing and solving project problems.
  - (7) Keeping the owner abreast of project operations.

- (8) Overseeing investment of project funds.
- (9) Ensuring that project positions are covered during vacations, sickness, and vacancies.

#### 6.50 Contracting Guidelines

- a. When an owner/agent is contracting for goods or services involving project income, an agent is expected to solicit written cost estimates from at least three contractors or suppliers for any contract, ongoing supply or service which is expected to exceed \$10,000 per year, or the threshold established by the HUD Area Office with jurisdiction over the project.
- b. For any contract, ongoing supply or service estimated to cost less than \$5,000 per year, the agent should solicit verbal or written cost estimates in order to assure that the project is obtaining services, supplies and purchases at the lowest possible cost. The agent should make a record of any verbal estimate obtained.
- c. Documentation of all bids should be retained as a part of the project records for three years following the completion of the work.

#### **Windridge Rent Collection Policy**

- 1. All rent must be paid by money order or check (NO CASH ACCEPTED) on or before the first (1<sup>st</sup>) day of each month and will be considered late after the fifth (5<sup>th</sup>) day.
- 2. All rent not paid by the fifth (5<sup>th</sup>) day of each month will be subject to a \$5.00 late fee on the sixth (6<sup>th</sup>) day of the month. Thereafter, management may collect \$1.00 for each additional day that rent remains unpaid during the month it is due. All rents not paid by the tenth (10<sup>th</sup>) of each month will result in eviction proceedings beginning on the eleventh (11<sup>th</sup>) day of the month.

Residents shall pay a service charge of \$30.00 on the second or each additional time a check is not honored for payment (bounces). It is a policy of Interstate Realty that we do not accept check from Residents after they have had two returned checks. **All rent must be paid by a money order or cashier's check after having two returned checks.**

- 3. At the time late charges are assessed (the close of the 5<sup>th</sup> day), a notice will be served in accordance with HUD regulations. This notice will allow ten (10) days for Lessee(s) to meet with the community manager and discuss the pending lease termination for non-payment of rent. In no way does this policy state or imply that additional time has been granted for payment of rent. All arrangements for deferred payments must be made prior to the time that rent is due on the 1<sup>st</sup> of each month
- 4. Seven (7) days from service of the initial notice of lease termination, a second notice will be served in accordance with the state law. This notice will allow three (3) days to vacate the premises. If the rent remains unpaid, legal action will be taken by the community office filing a forcible entry and detainer for possession of the premises and all rents are due. Failure to respond to this court summons and/or a decision for possession by the judge will require that you vacate the apartment and pay all charges and penalties awarded by the courts decision.

**NO RENT WILL BE ACCEPTED AFTER THE FORCIBLE ENTRY AND  
DETAINER HAS BEEN FILED, EXCEPT THROUGH THE DIRECTION OF  
THE COURT.**

5. As stated in item 3 above, all arrangements, for deferred payments must be made prior to the first of the month that rent is due. After the rent is delinquent, partial payments of rent cannot be accepted. All rents due must be paid in full. Any resident wishing to retain his/her rights of occupancy after the official three (3) day notice (required by the state) is served, must pay all delinquent rent, all late charges, all court costs (if any), and any damage charges. In addition, the rent for the following month must be paid.

After the forcible entry and detainer is filed, no payment will be accepted except as directed by the court. It is not the policy or practice of this apartment community to use local courts as a collection agency. Any court action filed for possession of the premises and all accrued charges permitted under state law. Any resident may present a legal defense at any hearing that affects his/her occupancy at said property.

**Windridge Landlord/Tenant Agreement**

**Paragraph 23**

**Termination of Tenancy:**

- a. To terminate this Agreement, the Tenant must give the Landlord 30-days written notice before moving from the unit.
- b. Any termination of this Agreement by the Landlord must be carried out in accordance with HUD regulations, State and local law, and the terms of this Agreement.
- c. The Landlord may terminate this Agreement for the following reasons:
  - (1) the Tenant's material noncompliance with the terms of this Agreement;
  - (2) the Tenant's material failure to carry out obligations under any State Landlord and Tenant Act;
  - (3) drug related criminal activity engaged in on or near the premises, by any tenant, household member, or guest, and any such activity engaged in on the premises by any other person under the tenant's control;
  - (4) determination made by the Landlord that a household member is illegally using a drug;
  - (5) determination made by the Landlord that a pattern of illegal use of a drug interferes with the health, safety, or right to peaceful enjoyment of the premises by other residents;
  - (6) criminal activity by a tenant, any member of the tenant's household, a guest or another person under the tenant's control:
    - (a) that threatens the health, safety, or right to peaceful enjoyment of the premises by other residents (including property management staff residing on the premises);
    - (b) or that threatens the health, safety, or right to peaceful enjoyment of their residences by persons residing in the immediate vicinity of the premises;
  - (7) if the tenant is fleeing to avoid prosecution, or custody or confinement after conviction, for a crime, or attempt to commit a crime, that is a felony under the laws of the place from which the individual flees or that in the case of the State of New Jersey is a high misdemeanor;
  - (8) if the tenant is violating a condition of probation or parole under Federal or State law;

- (9) determination made by the Landlord that a household member's abuse or pattern of abuse of alcohol threatens the health, safety, or right to peaceful enjoyment of the premises by other residents;
- (10) if the Landlord determines that the tenant, any member of the tenant's household, a guest or another person under the tenant's control has engaged in the criminal activity, regardless of whether the tenant, any member of the tenant's household, a guest or another person under the tenant's control has been arrested or convicted for such activity.
- d. The Landlord may terminate this Agreement for other good cause, which includes, but is not limited to, the tenant's refusal to accept change to this agreement. Terminations for "other good cause" may only be effective as of the end of any initial or successive term. The term material noncompliance with the lease includes: (1) one or more substantial violations of the lease; (2) repeated minor violations of the lease that (a) disrupt the livability of the project; (b) adversely affect the health or safety of any person or the right of any tenant to the quiet enjoyment to the leased premises and related project facilities, (c) interfere with the management of the project, or (d) have an adverse financial effect on the project (3) failure of the tenant to timely supply all required information on the income and composition, or eligibility factors, of the tenant household (including, but not limited to, failure to meet the disclosure and verification requirements for Social Security Numbers, or fail me to sign and submit consent forms for the obtaining of wage and claim information from State Wage Information Collection Agencies), and (4) Non-payment of rent or any other financial obligation due under the lease beyond any grace period permitted under State law. The payment of rent or any other financial obligation due under the lease after the due date but within the grace period permitted under State law constitutes a minor violation.
- e. If the Landlord proposes to terminate this Agreement, the Landlord agrees to give the Tenant written notice and the grounds for the proposed termination. If the Landlord is terminating this agreement for "other good cause," the termination notice must be mailed to the Tenant and hand-delivered to the dwelling unit in the manner required by HUD at least 30 days before the date the Tenant will be required to move from the unit and in accordance with State law requirements. Notices of proposed termination for other reasons must be given in accordance with any time frames set forth in State and local law. Any HUD required notice period may run concurrently with any notice period required by State or local law. All termination notices must:
- specify the date this Agreement will be terminated;
  - state the grounds for termination with enough detail for the Tenant to prepare a defense;
  - advise the Tenant that he/she has 10 days within which to discuss the proposed termination of tenancy with the Landlord.
- The 10-day period will begin on the earlier of the date the notice was hand-delivered to the unit or the day after the date the notice is mailed. If the Tenant requests the meeting, the Landlord agrees to discuss the proposed termination with the Tenant;
- and advise the Tenant of his/her right to defend the action in court.
- f. If an eviction is initiated, the Landlord agrees to rely only upon those grounds cited in the termination notice required by paragraph e.