



Rhode Island Housing Providence, RI

HOME Investment Partnerships Program



To: Robert D. Shumeyko
Director of Community Planning and Development, 1 CPD

From: //SIGNED//
Karen Campbell-Lawrence
Acting Regional Inspector General for Audit, 1AGA

Subject: Rhode Island Housing, Providence, RI, Did Not Always Adequately Support HOME Fund Expenditures

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Rhode Island Housing 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 (212) 264-4174.



Audit Report Number: 2015-BO-1002

Date: February 4, 2015

Rhode Island Housing, Providence, RI, Did Not Always Adequately Support HOME Fund Expenditures

Highlights

What We Audited and Why

We audited the Rhode Island Housing's HOME Investment Partnerships Program based on an Office of Inspector General risk assessment of New England HOME recipients that considered the amount of funding provided and prior audit and monitoring findings. Our audit objectives were to determine whether Rhode Island Housing officials awarded HOME funds to grantees in a reasonable and supported manner and whether HOME funds were disbursed in accordance with U.S. Department of Housing and Urban Development (HUD) rules and regulations.

What We Found

Rhode Island Housing officials disbursed HOME funds for questionable expenditures. Specifically, they disbursed HOME funds for (1) expenses incurred before the HOME agreement was executed, (2) expenses not included in the HOME agreement, (3) expenses that exceeded the budget allocation, and (4) an activity for which they did not obtain a deed restriction and support all of the costs incurred. In addition, officials executed a HOME agreement that did not comply with Federal regulations and approved a HOME application with inaccurate costs. We attributed these deficiencies to Rhode Island Housing officials' failure to maintain adequate supporting documentation and implement oversight controls over disbursements and contract execution. As a result, they could not assure HUD that reasonable and necessary costs were charged to the HOME program, and more than \$2.3 million in HOME funds was questioned.

In addition, officials did not always properly award and support HOME funds disbursed to community housing development organizations (CHDO). Specifically, for three CHDOs, charges for salary and operating expenses were not supported with adequate documentation. Thus, officials did not have sufficient controls to ensure adequate support for CHDO expenses and comply with HOME agreements and regulations. As a result, officials could not assure HUD that \$83,580 in HOME funds was allocated and disbursed in compliance with HOME requirements.

What We Recommend

We recommend that HUD require Rhode Island Housing officials to reimburse HUD \$887,544 from non-Federal funds for ineligible costs and provide support for more than \$1 million in costs. If sufficient support cannot be provided, officials should seek reimbursement from non-Federal funds and redistribute \$500,000 in HOME funds to other eligible HOME activities.

Table of Contents

Background and Objectives	3
Results of Audit	5
Finding 1: Rhode Island Housing Officials Disbursed HOME Funds for Questionable Expenditures	5
Finding 2: Rhode Island Housing Did Not Always Properly Support HOME Funds Disbursed to Its CHDOs	10
Scope and Methodology.....	12
Internal Controls.....	14
Appendixes.....	16
A. Schedule of Questioned Costs and Funds To Be Put to Better Use.....	16
B. Auditee Comments and OIG’s Evaluation	17
C. Schedule of Sampled HOME Units	28

Background and Objectives

Rhode Island Housing, a component of the Rhode Island Housing and Mortgage Finance Corporation of Providence, RI, was created by the Rhode Island General Assembly in 1973 as a privately funded public purpose corporation.

Rhode Island Housing's mission is to strive to ensure that all people who live or work in Rhode Island can afford a healthy, attractive home that meets their needs. To achieve its mission, Rhode Island Housing offers lending programs, provides housing-related education to consumers and others, promotes and finances sensible development that builds healthy and vibrant communities, provides housing grants and subsidies, and teams up with partners to improve everything it does.

In May 2006, the governor of Rhode Island sent a letter to the U.S. Department of Housing and Urban Development's (HUD) Office of Community Planning and Development, explaining that Rhode Island Housing would act on behalf of the State of Rhode Island to administer funding under the HOME Investment Partnerships Program. In addition, Rhode Island Housing's executive director and his designees were authorized to contract with HUD to administer the HOME program and ensure compliance with regulations at 24 CFR (Code of Federal Regulations) Part 92. Rhode Island Housing is overseen by a seven-member board of commissioners, which generally meets monthly.

The HOME program provides formula grants to States and localities that communities use, often in partnership with local nonprofit groups, to fund a wide range of activities, including building, buying, and rehabilitating affordable housing for rent or home ownership or providing direct rental assistance to low-income people.

HOME is the largest Federal block grant to State and local governments designed exclusively to create affordable housing for low-income households.

Rhode Island Housing received and used HOME funds as follows:

Funding period	HOME funding received	Affordable homes created
March 1, 2010, to February 28, 2011	\$5,491,919	118
March 1, 2011, to February 29, 2012	\$4,846,572	77
March 1, 2012, to February 28, 2013	\$3,073,000	98
Totals	\$13,411,491	293

Our audit objectives were to determine whether Rhode Island Housing officials awarded HOME funds to grantees in a reasonable and supported manner, and disbursed HOME funds in accordance with HUD rules and regulations.

Results of Audit

Finding 1: Rhode Island Housing Officials Disbursed HOME Funds for Questionable Expenditures

Contrary to Federal requirements, Rhode Island Housing officials disbursed HOME funds for questionable expenditures. Specifically, they disbursed HOME funds for (1) expenses incurred before the HOME agreement was executed, (2) expenses not included in the HOME agreement, (3) expenses that exceeded the budget allocation, and (4) an activity for which they did not obtain a deed restriction and support all of the costs incurred. In addition, officials executed a HOME agreement that did not comply with Federal regulations and approved a HOME application with overstated costs. We attributed these deficiencies to Rhode Island Housing's failure to maintain adequate supporting documentation and implement oversight controls over disbursements and contract execution sufficient to ensure compliance with applicable regulations. As a result, Rhode Island Housing officials could not assure HUD that reasonable and necessary costs were charged to the HOME program, and more than \$2.3 million in HOME funds was questioned.

Eighteen HOME Activities Were Reviewed

We reviewed 18 HOME activities initiated between March 1, 2010, and February 28, 2013. We determined that 14 of the 18 activities, or 77 percent, had more than \$2.3 million in questioned costs, of which \$883,092 was ineligible, more than \$1 million was unsupported, and \$500,000 represented funds that could be put to better use. Appendix C lists the 18 HOME activities reviewed, and the details are described below.

Costs Incurred Before the HOME Agreements Were Ineligible

For four HOME activities, \$883,092 in costs was incurred months or years before the HOME agreements were signed. Section 5 of the HOME agreements prohibits recipients from starting all or any part of the approved activity or incurring or becoming obligated with respect to any costs before the recipient's execution and delivery of the loan documents and notice to proceed. For activity number 4996, a HOME agreement was executed on July 10, 2012, totaling \$500,000, which included a budget for \$400,000 in construction costs and \$100,000 in contingency costs. However, the developer sought reimbursement for \$400,000 in construction costs for the period ending April 30, 2012, which was approximately 2½ months before the HOME agreement was signed. Therefore, the \$400,000 was ineligible.

For activity number 5023, a HOME agreement was executed on December 20, 2012, totaling \$260,000, which included a budget for \$200,000 in acquisition costs, \$30,000 in construction costs, and \$30,000 in contingency costs. However, the developer sought reimbursement for \$44,759, consisting of \$6,180 in relocation expenses, \$31,867 in loan interest, and \$6,712 for a developer's fee. Not only were these items not included in the approved budget, the costs were incurred 9 to 10 months before the HOME agreement was signed. Therefore, the \$44,759 was ineligible.

For activity number 4592, a HOME agreement was executed on February 28, 2011, totaling \$450,000, which included a budget for \$405,000 in architectural and engineering costs and \$45,000 in legal, soft, and financing costs. Further, there was an amendment that included an additional \$50,000 in legal, soft, and financing costs. However, the developer sought reimbursement for \$437,574, of which \$388,749 (construction and environmental services and predevelopment loans) was incurred before the HOME agreement was signed and, therefore, was ineligible and \$62,426 consisted of unsupported additional construction costs incurred that were not included in the budget.

For activity number 4320, a HOME agreement was executed on October 30, 2009, totaling \$675,000 for various costs. The developer sought reimbursement for \$49,584, consisting of \$22,000 in architectural and engineering costs and \$27,584 in construction costs. Although in some cases, HUD may allow for reimbursement of architectural and engineering costs incurred 18 months before the HOME agreement is signed, in this case, the costs were incurred between May and August 2005, more than 4 years before the agreement was signed. Similarly, the construction costs were incurred in 2005-2006, 3 to 4 years before the HOME agreement was signed. Therefore, \$49,584 was ineligible.

Costs Were Not Included in the HOME Agreement Budgets

For seven HOME activities (see appendix C), there were costs that were not included in the HOME agreement budgets. Section 5 of the HOME agreements provides that the recipient agrees that the approved activity must be carried out in accordance with the budget set forth in attachment A. The budgets stated that “the recipient shall use the proceeds of the Advances solely for the following purpose” and provides the breakout of expenses covered with HOME funds and other funding. Therefore, reimbursement should be sought only for expenses agreed upon in the executed written agreement or an amendment.

For activity number 4596, the HOME agreement was signed on March 2, 2011, not to exceed \$80,000, and the budget allocated the entire \$80,000 HOME award for acquisition. However, the entire \$80,000 was drawn down and used for expenses other than acquisition (developer’s fee – \$22,946, construction – \$38,191, and contingency – \$18,863); therefore, these costs were unsupported. In another example, for activity number 5000, the HOME agreement was signed on August 18, 2012, for \$140,000. According to the HOME agreement budget, \$90,000 was for contingency, and \$50,000 was for soft costs (relocation costs, financing fees, legal and accounting fees, architectural and engineering services, and other reasonable and necessary costs), and any amendments to this budget were required to be approved by Rhode Island Housing in writing before adoption. However, \$139,138 was paid for a developer’s fee. Since the budget did not allocate HOME funds for developer’s fees and there was no amendment, these costs were considered to be unsupported as they were not paid according to the agreement and respective budget.

Costs Exceeded the Budgets

For 11 HOME activities (see appendix C), there were costs of \$994,257, which exceeded the allocated amounts approved in the HOME agreements and were unsupported. Although the expenditures reviewed were supported by backup documentation, deviations from the agreed-

upon HOME agreement budgets could have allowed multiple funding sources to pay for the same reimbursable costs. Therefore, a review of the total sources and uses of funds may be necessary to determine whether these deviations from the agreed-upon budgets resulted in duplicative or excessive payments of Federal funds (that is, the Federal Government and another entity paying for the same expenses).

For example, for activity number 4760, the HOME agreement stated that the recipient was required to use the proceeds of the advance solely for the following purposes:

Cost category	HOME budget
Architecture and engineering	\$63,060
Contingency	\$85,080
Developer's fee	\$125,000
Soft costs	\$26,860
Total	\$300,000

The agreement further provided that amendments to the budget were required to be approved by Rhode Island Housing officials in writing before adoption. Based on the support in the files, \$179,436 and \$42,020 were drawn down for contingency (funds held for cost overruns) and soft costs, respectively, which exceeded the amounts budgeted for these items by \$109,516 (\$94,356 under contingency and \$15,160 for soft costs). Since the amount disbursed for contingency and soft costs exceeded the budgeted amounts according to the HOME agreement and there was no approved amendment, these costs were unsupported.

Deed Restriction and Costs Were Not Supported

Activity number 4511 was awarded \$940,000 in HOME funds for 20 very low-income units and was completed in January 2013. Despite having been completed for more than a year, the units did not have an executed deed restriction. Without a deed restriction in place, there was no assurance that the 20 HOME-assisted units would remain affordable for the next 40 years as required. After the exit conference, Rhode Island Housing officials submitted evidence that a deed restriction was recorded in May 2014. However, they could not provide support for \$1,839 associated with two drawdown requests totaling \$48,865 (voucher number 5466691 for \$1,339 and voucher number 5511794 for \$500) for construction, engineering, and landscaping services.

HOME Agreements Did Not Comply With Regulations

For activity number 4594, Rhode Island Housing officials did not ensure that the rents charged complied with HOME requirements. According to 24 CFR 92.252(d), the initial rent schedule and utility allowances must establish the maximum monthly allowances for utilities and services (excluding telephone). The participating jurisdiction must review and approve rents proposed by the owner. Further, if the owner or developer undertakes rental projects, the written agreement must establish the initial rents and the procedures for rent increases. However, when we reviewed the written agreements for this activity, they did not include an approved initial rent schedule and utility allowances, nor did they include procedures for rent increases. Thus, Rhode

Island Housing officials did not operate the program in compliance with HOME regulations, and two unit rents exceeded the maximum amount that could be charged. As a result, rental overpayments of \$4,452 were made to the landlord by either the tenants or the Section 8 program (see chart below).

Unit no.	HOME rent limit	Gross rent	Excess rent	Number of months charged	Unsupported excess rent charged
1	\$968	\$1,161	\$193	12	\$2,316
2	\$983	\$1,161	\$178	12	\$2,136
Total					\$4,452

An Applicant Overstated the Acquisition Cost of a Property

An application for activity number 5021 should not have been awarded \$500,000 in HOME funds because the information in the application was inaccurate. The applicant submitted an application in January 2012, proposing to develop 40 2- and 3-bedroom units for working families, stating that the acquisition cost of the rehabilitated property was \$1.2 million. However, the applicant purchased the mostly vacant property in December 2007 for \$900,000. Thus, the applicant overstated the value of the property by \$300,000. Since the application incorrectly stated the acquisition cost, the applicant should not have been awarded HOME funds. As part of the HOME application process, the applicant signed the agreement and certification, which stated that the information in the application was true and correct. However, while the applicant was incorrectly awarded \$500,000 in HOME funds, the project was stalled, and no HOME were expended due to legal matters.

Conclusion

Rhode Island Housing officials disbursed HOME funds for questionable expenditures, executed a HOME agreement that did not comply with regulations, and approved a HOME application that contained inaccurate information. We attributed these deficiencies to Rhode Island Housing officials' failure to maintain adequate supporting documentation and implement oversight controls over disbursements and contract and grant application execution sufficient to ensure compliance with applicable regulations. As a result, Rhode Island Housing officials disbursed more than \$2.3 million in HOME funds for ineligible and unsupported expenditures and could not assure HUD that reasonable and necessary costs were charged to the HOME program and that the program was administered in accordance with program regulations.

Recommendations

We recommend that the HUD Director of Community Planning and Development instruct Rhode Island Housing officials to

- 1A. Reimburse HUD from non-Federal funds for the \$883,092 in ineligible costs incurred before the HOME agreements were executed.
- 1B. Provide support for \$994,257 related to the 11 HOME activities in which the costs were not included in the budget or exceeded the allocated amounts approved in the HOME agreement (appendix C). If support cannot be provided, officials should reimburse HUD from non-Federal funds for the unsupported amount.
- 1C. Provide support for the \$1,839¹ in unsupported costs associated with activity number 4511. If support cannot be obtained, this amount should be reimbursed from non-Federal funds.
- 1D. Determine whether the tenants or the Section 8 program overpaid rents for activity number 4594 and if so, reimburse the affected party by \$4,452.
- 1E. Deobligate the \$500,000 in HOME funds allocated to activity number 5021 because the application contained inaccurate cost information.
- 1F. Develop and implement policies and procedures to ensure that all HOME funds disbursed are for eligible costs associated with an activity that has an approved written HOME agreement.
- 1G. Develop and implement policies and procedures to ensure that written HOME agreements comply with Federal rules and regulations and rents comply with HUD regulations.

¹ This \$1,839 is part of the \$940,000 questioned in 1C.

Finding 2: Rhode Island Housing Did Not Always Properly Support HOME Funds Disbursed to Its CHDOs

Rhode Island Housing officials did not always properly award and support HOME funds disbursed to community housing development organizations (CHDO). Specifically, for three CHDOs, charges for salary and operating expenses were not supported with adequate documentation to justify the expenses. Rhode Island Housing officials did not have sufficient controls to ensure adequate support for CHDO expenses and compliance with HOME agreements and regulations. As a result, they could not assure HUD that \$83,580 in HOME funds was allocated and disbursed in compliance with HOME requirements.

CHDO Costs Were Not Adequately Supported

We reviewed CHDO costs for six activities and determined that three were adequately supported and three were not. Specifically, \$83,580 of \$139,265 in incurred costs (60 percent) was not properly supported and allocated. For example, one CHDO submitted payroll records for the quarters ending December 31, 2011, and March 31, 2012, for a total of \$15,888. A Rhode Island Housing official approved a check request form for \$7,944 on March 20, 2012, and a second a check request form for the same amount on October 23, 2012. However, although the employees' time cards showed \$54,719 in salary, which is significantly greater than the amount requested for reimbursement, Rhode Island Housing officials could not support the allocation of the \$15,888. As a result, there was no assurance that these CHDO salary costs should have been charged to the HOME program. Therefore, HUD had no assurance that the employees worked on a CHDO activity and that expenses were reasonable and necessary.

In another instance, \$24,000 in CHDO operating funds was drawn down without sufficient supporting documentation. The only document available was the CHDO operating funds agreement. Further, Rhode Island Housing officials approved operating expenses of \$43,692 on March 27, 2012, to another CHDO, and the only documentation available was a budget comparison report. Without adequate documentation to support the charges, there was no assurance that the expenses were reasonable and necessary.

Regulations at 24 CFR 92.208(a) provide that operating expenses are reasonable and necessary costs for the operation of a CHDO. Such costs include salaries and other employee compensation and benefits; employee education, training and travel; rent; utilities; communication costs; taxes; insurance; equipment; materials; and supplies. Additionally, 24 CFR 85.20(b)(6) states that records must be supported by source documentation, such as canceled checks, paid bills, payrolls, time and attendance records, and contract and subgrant award documents. The documentation provided by Rhode Island Housing officials for the \$83,580 in CHDO operating expenses was not adequate. Therefore, these expenses may not have been reasonable and necessary and chargeable to the HOME program.

Conclusion

Rhode Island Housing officials did not always support HOME disbursements made to CHDOs. Specifically, for three CHDOs, charges for salaries and operating expenses were not adequately supported. This condition occurred because Rhode Island Housing officials did not have

sufficient controls to ensure adequate support for CHDO expenses and comply with regulations and HOME agreements. As a result, they could not assure HUD that \$83,580 in HOME funds was allocated or disbursed in compliance with HOME requirements.

Recommendations

We recommend that the HUD Director of Community Planning and Development instruct Rhode Island Housing officials to

- 2A. Provide support for the unsupported \$83,580 in salaries and operating expenses. If proper support cannot be provided, officials should repay this amount to HUD from non-Federal funds.
- 2B. Develop and implement policies and procedures to ensure that CHDO salary and operating expenses are reasonable and necessary and that costs are properly supported before disbursement.

Scope and Methodology

We performed our onsite audit work at Rhode Island Housing's main office located at 44 Washington Street, Providence, RI, from October 2013 to April 2014. Our audit generally covered the period March 1, 2010, through February 28, 2013, and was extended when necessary to meet our audit objectives. We used computer-processed data and verified the data by reviewing hardcopy supporting documentation or other data from a different source. We found the data to be adequate for our purposes.

To accomplish our objectives, we

- Reviewed applicable laws, regulations, HUD handbooks, HUD notices, and Rhode Island Housing's policies and procedures.
- Conducted discussions with Rhode Island Housing officials to gain an understanding of Rhode Island Housing's financial structure and administration of the HOME program.
- Reviewed records of Rhode Island Housing's board minutes, independent public auditor's reports, and monitoring reviews by HUD.
- Reviewed Rhode Island Housing's action plans and consolidated annual performance and evaluation reports for 2010, 2011, and 2012.
- Reviewed various Integrated Disbursement and Information System² reports.
- Determined whether Rhode Island Housing allocated HOME funds in a reasonable and supported manner.
- Determined whether tenants who were residing in selected units were income eligible.
- Determined whether rents charged to tenants met HOME program requirements.
- Selected a nonstatistical sample of activities to test from a listing of HOME activities provided by Rhode Island Housing. During the period March 1, 2010, through February 28, 2013, there were 29 agencies, and they committed more than \$12.1 million for 69 activities. We subdivided the 29 agencies into three categories: (1) those that received

² Integrated Disbursement & Information System is a nationwide database that provides HUD with current information regarding program activities and is the drawdown and reporting system for several programs, including the HOME program.

\$500,000 or more (11 agencies), (2) those that received \$200,000 but less than \$500,000 (10 agencies), and (3) those that received less than \$200,000 (8 agencies). We then selected 8 activities from the first category, 5 activities from the second category, and 5 activities from the third category for a combined total of 18 activities. Our results apply only to the activities selected. The 18 activities are identified in appendix C.

- Performed onsite inspections for selected activities to determine whether they met housing quality standards.

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.

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:

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that the use of program funds is consistent with laws and regulations.
- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that funds are safeguarded against waste, loss, and misuse.

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:

- Rhode Island Housing officials did not have adequate controls over compliance with laws and regulations when they did not ensure that costs submitted were (1) incurred after the written agreements were approved and signed and (2) in accordance with and did not exceed the budget. Also, Rhode Island Housing officials did not ensure that HOME rents complied with rules and regulations and deed restrictions were obtained (see finding 1).
- Rhode Island Housing officials did not have adequate controls over safeguarding resources when they (1) used HOME funds to pay for costs submitted by organizations, which were not in accordance with the signed HOME agreements; (2) paid CHDO operating expenses that were not necessary, reasonable, and supported; and (3) allocated funds for a HOME application in which the applicant had inflated the acquisition cost of a property by \$300,000 (see findings 1 and 2).

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	\$883,092		
1B		\$994,257	
1C		\$1,839	
1D		\$4,452	
1E			\$500,000
2A		\$83,580	
Totals	\$883,092	\$1,084,128	\$500,000

- 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 Office of Inspector General (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 Rhode Island Housing officials deobligate the \$500,000 related to activity number 5021 because the application contained inaccurate cost information and the project was stalled, those funds could be used on another HOME project.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments



Rhode Island Housing
working together to bring you home

RICHARD H. GODFREY, JR.
EXECUTIVE DIRECTOR

VIA ELECTRONIC MAIL
AND FIRST CLASS MAIL

December 15, 2014

Mr. Edgar Moore
Regional Inspector General for Audit
U.S. Department of HUD-Office of Inspector
General for Audit
26 Federal Plaza, Room 3430
New York, NY 10278-0068

Dear Mr. Moore:

Thank you for the opportunity to comment on the OIG Audit Report Number 2015-BO-100X (the "Audit Report") of Rhode Island Housing's HOME Investment Partnerships Program (the "Program"). We appreciate the work of the OIG in evaluating the Program and are always seeking ways to improve our partnership with HUD. Rhode Island Housing officials are pleased to have administered \$98 million in federal HOME Program funding since program inception to provide more than 4,400 affordable homes for low- and very low-income individuals and families.

Rhode Island Housing believes that it has administered the State HOME Program for the State of Rhode Island in full compliance with HUD regulations. Rhode Island Housing has disbursed funding for eligible project expenses upon execution of HOME Agreements; has disbursed HOME funding for eligible expenses in accordance with 24 CFR Part 92; and has documented evidence of deed restrictions for each HOME-assisted development that complies with HUD regulations. Rhode Island Housing officials have implemented the State HOME Program with adequate oversight controls and HOME Program funding was used for eligible activities in providing affordable housing opportunities for low- and very low-income Rhode Islanders. We look forward to working with HUD CPD staff to resolve the issues outlined in the Audit Report.

Response to Audit Report Number 2015-BO-100X

Finding 1: Rhode Island Housing Officials Disbursed HOME Funds for Questionable Expenditures

The Audit Report identified items that are classified as "questionable expenditures" which fall into the following six categories:

1. Expenses incurred before the HOME Agreement was executed.
2. Expenses not included in the HOME Agreement.

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Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 1

Mr. Edgar Moore
December 15, 2014
Page 2

3. Expenses that exceeded the budget allocation.
4. An activity for which a deed restriction, and support for costs incurred, was not obtained.
5. Improper HOME Agreement
6. HOME application with overstated costs

These items were further broken down into eight recommendations. Each of the recommendations are addressed below.

1A. Reimbursement of expenses incurred before HOME Agreements were executed

The Audit Report notes that in the case of four HOME activities, HOME funds were used for expenses incurred before the HOME Agreement was executed, and concludes that these expenses are therefore not HOME-eligible expenses. This conclusion is not required by the applicable HOME regulations.

24 C.F.R. §92.504(b) sets forth HUD's requirements regarding the interplay between execution of a HOME Agreement and payment of expenses. This section reads as follows:

Executing a written agreement. Before disbursing any HOME funds to any entity, the participating jurisdiction must enter into a written agreement with that entity. Before disbursing any HOME funds to any entity, a State recipient, subrecipient, or contractor which is administering all or a part of the HOME program on behalf of the participating jurisdiction, must also enter in a written agreement with that entity. The written agreement must ensure compliance with the requirements of this part. (Emphasis added.)

This section does not prohibit reimbursement for expenses incurred prior to the execution of the HOME Agreement; rather, it merely requires that prior to disbursement of HOME funds a written agreement must be in place. That requirement makes sense. HOME funds ought not to be disbursed before the receiving entity agrees to the requirements of the HOME program; however, once that commitment has been made, there is no prohibition on using HOME funds to cover expenses incurred prior to the execution of the HOME Agreement, assuming that those expenses are eligible expenses under the HOME Program.

In all four cases cited in the Audit Report it is evident that no HOME funds were disbursed prior to the execution of the HOME Agreement. The following chart sets forth the date of execution of the HOME Agreement and the first date of disbursement of HOME funds.

Activity Number	Date of Agreement	Date of Disbursement
4996	July 10, 2012	July 17, 2012

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Mr. Edgar Moore
December 15, 2014
Page 3

5023	December 20, 2012	September 9, 2013
4592	February 28, 2011	March 3, 2011
4320	October 30, 2009	November 30, 2009

Furthermore, HUD regulations explicitly recognize that in some instances HOME funds may be used for payment of eligible costs incurred before the effective date of the HOME Agreement. See 24 C.F.R. §212(a)

Before the effective date of the HOME Investment Partnership Agreement, the participating jurisdiction may incur costs which may be charged to the HOME allocation after the award of the HOME allocation, provided the costs are in compliance with the requirements of this part (including environmental review requirements) and with the statutory and regulatory requirements in effect at the time the costs are charged to the HOME allocation.

Thus, the conclusion in the Audit Report that any expenses incurred prior to the execution of the HOME Agreement is "ineligible" merely based on the timing of the expense is incorrect under these HUD regulations.

Finally, in each of these cases, all HOME funds were used for expenses that are eligible activities as defined in 24 C.F.R. Part 92, Subpart E, Eligible and Prohibited Activities.

Rhode Island Housing staff will review these four activities with HUD CPD and provide additional information and documentation with respect to the costs and payments.

1B. Provide support for \$994,257 related to HOME activities in which costs were not included in, or exceed the allocated amounts in the HOME Agreement

The Audit Report concludes that for eleven HOME activities, HOME funds were used either for expenses either (i) not included in, or (ii) in excess of the HOME Agreement budget. The Audit Report classifies these amounts as unsupported. Rhode Island Housing contends that all of these expenses are eligible expenses within the definition of applicable HUD regulations, and in no case did the HOME funds disbursed for a particular activity exceed the HOME award committed under the HOME Agreement. Therefore, no reimbursement should be required.

24 C.F.R. §92.504(c)(1)(i) provides that "The agreement must describe the use of the HOME funds, including the tasks to be performed, a schedule for completing the tasks, and a budget. These items must be in sufficient detail to provide a sound basis for the State to effectively monitor performance under the agreement. Rhode Island Housing has met these requirements.

By its very nature, the real estate development process is fluid. It is not unusual for budget projections developed at the initiation of a project to change over time as the

Comment 2

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Mr. Edgar Moore
December 15, 2014
Page 4

development progresses and more information becomes available. This was precisely the situation regarding the HOME activities identified in the Audit Report. At every stage of the process, Rhode Island Housing was aware of the changes in the budgets, the nature of the expenses paid with HOME funds, and the overall sources and uses of the entire development budget. It may have been better practice to execute a budget amendment for each change; however, as long as the current expenses to be paid from HOME funds were monitored to ensure that they comprise eligible expenses and that, in the aggregate they do not exceed the HOME award specified in the HOME Agreement, the HUD requirements dealing with budgets in the HOME Agreement are met.

Rhode Island Housing staff has complete master payoff sheets for each of these projects and will provide additional information and documentation to HUD supporting the \$994,257 in eligible HOME expenses related to costs for 11 HOME assisted developments.

Four of these activities are categorized as "Cost exceed budget" in Appendix C to the Audit Report. In no instance did the actual HOME expenditure exceed the HOME award – these "excessive costs" reflect higher than anticipated disbursements or cost overruns within various line-items associated with the development process. For example, the applicant for activity number 4520 estimated in its application an acquisition of \$80,000 for property acquisition within an overall HOME budget of \$160,000. The applicant and project was approved by the Rhode Island Housing Board of Commissioners and a HOME Agreement and budget reflecting the \$80,000 acquisition was executed. Subsequent to the execution of the HOME Agreement, the applicant entered into a purchase and sales agreement for the property in the amount of \$85,000. The HUD Settlement Statement supports the \$85,000 contract sales price. This increased acquisition cost included escrow of real estate taxes, attorney settlement charges and water and sewer charges. As a result of the increased acquisition cost of \$5,000 there was a corresponding decrease of another line item within the budget. All expenditures were for eligible development activities in accordance with HUD regulations for the HOME Program at 24 C.F.R §§ 92.205 and 92.206.

An additional five activities were in two categories in Appendix C: "Cost exceed budget" and "Cost not in budget". The budget referred to by the OIG is the budget in the HOME Agreement, a document signed immediately following funding approval by the Rhode Island Housing Board of Commissioners, environmental clearance and HUD approval of a Request for Release of Funds. As described above, individual line items within the HOME Agreement budget may differ slightly from the project allocation of costs among sources and uses of funds as a result of such factors as changes or delays in other project funding sources, actual construction bids versus construction cost estimates, development team value engineering of construction costs and increases or reductions to soft costs associated with the development.

All variances in costs are captured within the project master payout sheets. Staff closely monitors project progress and budget changes. When staff reviews any variance it evaluates the variance with respect to reasonableness and necessity of cost. Any change

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 3

Mr. Edgar Moore
December 15, 2014
Page 5

made to the project master payout by Rhode Island Housing implicitly constitutes budget amendments. Rhode Island Housing officials assert that it is appropriate to require that master payout sheets reflect all actual payments and indicate variance between estimated costs and actual development-related expenses. All expenditures and drawdowns approved by Rhode Island Housing officials were for eligible expenses in compliance with HUD regulations at 24 C.F.R. §§92.205 and 92.206.

Rhode Island Housing has established a new policy of allowing payment for only those line-item costs as budgeted in the HOME Agreement unless an applicant provides a written request for a modification. The applicant must justify the necessity and cost reasonableness associated with the requested modification. Rhode Island Housing officials will document approved changes in the project file. Costs that exceed budget line-items will continue to be appropriately evidenced on the master payout sheets to ensure that staff can adequately monitor variance in budget line items.

Staff will provide additional documentation to HUD CPD staff and discuss any additional recommended corrective actions.

- 1C. Lack of Deed Restriction
- 1D. Unsupported expenses

Both of these recommendations relate to activity number 4511, which was financed in part with HUD Section 202 Supportive Housing for the Elderly Program ("Section 202") funding. Upon completion of the project in February 2014, the project sponsor executed the standard deed restriction that Rhode Island Housing typically uses in our HOME transactions. However, Rhode Island Housing was informed by Providence HUD legal counsel that we would not be permitted to record a HOME deed restriction on the property due to the existence of the Section 202 financing on the property.

Rhode Island Housing legal counsel engaged with CDP representative [REDACTED] and HUD multifamily attorney [REDACTED] to secure authorization to record the HOME deed restriction in accordance with HUD regulations. On April 22, 2014 Rhode Island Housing received approval to record the restriction and in June 2014 recorded the restriction ensuring the long-term affordability of the 20 HOME assisted units. A pdf copy of relevant emails with HUD entitled Activity 4511 deed restriction and the executed and recorded Deed Restriction entitled Activity 4511 recorded restriction is provided as evidence to this matter. Rhode Island Housing was aware of the obligation to record a deed restriction, and as evidenced by the attached correspondence did everything in its power to accomplish the recording. The only reason that the deed restriction was not recorded earlier was the unwarranted resistance by HUD's counsel to the filing of the document.

The Audit Report states that Rhode Island Housing could not provide support for drawdowns numbered 5466691 and 5511794 in the amount of \$1,339 and \$500 respectively. In fact, both vouchers were fully supported by eligible expense documentation and Rhode Island Housing staff disbursed payment in accordance with

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 4

Mr. Edgar Moore
December 15, 2014
Page 6

HUD regulations. The applicant requested final project payment of \$47,865.03 but only provided \$44,715.91 in acceptable documentation for the drawdown numbered 5466691. Rhode Island Housing staff allowed payment of only \$42,865.03 of the requested project payment and reserved the balance of HOME funding available for payment of eligible expenses until receipt of HUD required closeout documentation from the applicant.

Upon submittal of the required closeout documentation, the applicant submitted a request for payment for the balance of HOME funding. The applicant resubmitted for the unpaid expenses associated with the retainage held by Rhode Island Housing staff under voucher numbered 546691 in addition to other supporting documentation for \$4,000 in eligible project expenses. In both instances, the applicant submitted supporting documentation that far exceeded the HOME funding disbursed by Rhode Island Housing officials.

For the above reasons, Rhode Island Housing disagrees with the OIG's finding that Deed Restrictions and Costs Were Not Supported. In addition, as this matter only involves one activity numbered 4511, Rhode Island Housing requests that any reference that is included in this report should be singular versus plural form.

1E. Determination that rents were overpaid

The Audit Report concluded that Rhode Island Housing did not ensure that rents charged for activity number 4594 complied with HOME requirements. This conclusion is incorrect.

Rhode Island Housing provides guidance to applicants on the appropriate maximum rents and utility allowances related to each development in the initial application materials for underwriting purposes, at project completion and on an annual basis as income and rent are adjusted by HUD for the HOME Program. This information is provided upon submission of the final request for payment by an applicant for a development. Clear guidance as to the maximum allowable income for residents and HOME rent is referenced in the conditions of each HOME Agreement and is further referenced in the recorded Deed Restriction.

The OIG may have misinterpreted the information provided within the closeout file for activity number 4594. The rent and utilities charged by the applicant to each resident is in compliance with HOME regulations and the requirements set forth in the HOME Agreement and Deed Restriction. Total rent and utilities for each resident does not exceed 30% of each resident's income. Accordingly, the residents did not overpay the applicant for their portion of the required rent.

However, because this property is assisted under the Section 8 Program, the applicant received a Housing Assistance Payment from the local housing authority that exceeded the maximum permitted under the HOME requirements. The applicant corrected its calculation of gross rent in 2013 to comply with the HOME Agreement, Deed Restriction and HOME regulations. This excess payment was from the housing authority

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 5

Mr. Edgar Moore
December 15, 2014
Page 7

and not from the residents. At no time did residents pay any amount in excess of the maximum permitted under the HOME program.

In order to prevent this situation from recurring, Rhode Island Housing will provide additional guidance and assistance to applicant/owners of developments that provide affordable homes for residents that participate in the Section 8 Housing Choice Voucher Program to ensure that total rent collected is within the guidelines set forth in the HOME Agreement, Deed Restriction and HOME regulations. As this issue was limited to one activity number 4594, Rhode Island Housing requests that the reference to this deficiency be in singular form versus plural.

1F. Inaccurate cost information.

The Audit Report concludes that the applicant set forth inaccurate cost information relating to acquisition costs in its application. Rhode Island Housing disagrees with the OIG calculation of acquisition cost.

The applicant correctly projects and stated the acquisition cost of the property within its HOME application. Project number 5021 is a 40 unit housing tax credit development with a total projected development cost greater than \$10 million. The primary source of financing for the development is housing tax credit equity in excess of \$8.2 million.

The Audit Report correctly notes that the applicant acquired the property in 2007 at a sales price of \$900,000. However, the Audit Report incorrectly assumes that the "acquisition cost" for purposes of the tax credit development, which is the project for which the HOME application was submitted, is the same as the price paid in 2007.

Tax credit developments are typically undertaken by a single-purpose limited partnership or limited liability corporation. The real estate will be transferred from the applicant, who acquired the property in 2007, to the newly-formed LP or LLC. The price that will be paid by the LP or LLC is equal to the \$900,000 acquisition cost paid by the applicant in 2007, plus all of the intermediate costs directly related to the property since 2007, including accrued interest on the acquisition financing and carrying costs of the land for the period of 2007 through the projected closing date in late 2012, such as insurance, taxes and the like.

Over the seven years since the applicant initially acquired the property these carrying costs would be significant, and would be included in the project financing for the tax credit transaction. Rhode Island Housing has documented and verifiable evidence regarding the original acquisition cost, plus the interim carrying costs, which supports the applicant's presentation and certification of information set forth within its HOME Agreement. These are all eligible costs under 24 C.F.R. §§92.206 (c) and (d). Evidence of the acquisition cost is attached in pdf form, Activity 5021 Payoff Statement and Activity 5021 Acquisition Closing Statement.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 6

Mr. Edgar Moore
December 15, 2014
Page 8

Due to ongoing neighborhood opposition and protracted litigation the project has been unable to proceed. While we believe that this application properly presented anticipated acquisition cost information, due to the continued litigation we agree that this project is likely unable to proceed anytime soon. Therefore, Rhode Island Housing will accept the recommendation to deobligate the HOME award. Accordingly, the \$500,000 in HOME funding and other funding commitments such as housing tax credits have been de-obligated. The activity has been canceled by HUD.

- 1G. Develop policies and procedures regarding disbursement
- 1H. Develop policies and procedures regarding HOME Agreements

Rhode Island Housing has policies and controls in place to ensure that HOME funds are disbursed for eligible HOME expenditures in accordance with 24 C.F.R. §§92.206 and 92.207. Rhode Island Housing has reviewed its policies and controls and has implemented appropriate changes to ensure that all HOME funds are disbursed for eligible costs in accordance with HOME Agreement budgets. In May 2014, Rhode Island Housing conducted a workshop for applicants to review this revised policy, as well as other changes to the HOME Program related to the FY 2012 HOME Appropriations Law requirements and the 2013 HOME Final Rule. Rhode Island Housing will amend budgets as necessary for eligible HOME expenditures, if appropriate.

Rhode Island Housing also has policies and procedures in place that ensures that written HOME Agreements comply with Federal rules and regulations and that the existing policies and procedures ensure that rents are consistent with HUD regulations. In addition, Rhode Island Housing employs a team of compliance staff that conducts ongoing monitoring of HOME assisted projects to ensure that owners/sponsors continue to comply with HOME Agreements, Deed Restrictions and Federal rules and regulations.

Finding 2: Rhode Island Housing Did Not Always Properly Support HOME Funds Disbursed to Its CHDOs

The Audit Report concluded that CHDO costs were not always adequately supported. The Audit Report contained two recommendations regarding this finding. Each will be addressed in turn.

2A. Provide support of \$83,580 in CHDO salaries and operating expenses

Rhode Island Housing maintains that funding for eligible Community Housing Development Organizations ("CHDOs") was properly awarded and supported in compliance with 24 C.F.R. §92.208 which sets forth HUD regulations for CHDO operating expense and capacity building costs. In addition, Rhode Island Housing asserts that there is adequate supporting documentation within the three CHDO files referenced by the OIG to justify payment of \$83,580 to these CHDOs for reasonable and necessary expenses.

Comment 7

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 8

Mr. Edgar Moore
December 15, 2014
Page 9

The three CHDO payments questioned in the OIG Report are all documented with source documents such as time sheets and wage payments, utility bills, rent payments, income and expense budget summaries, and the like. These are all eligible CHDO operating expenses under 24 C.F.R. § 92.208.

2B. Develop and implement policies and procedures regarding CHDO salary and operating expenses

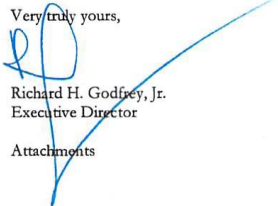
Rhode Island Housing has established CHDO policies and procedures in accordance with 24 C.F.R. §92.208. Rhode Island Housing provides CHDO operating funds in direct relation to the CHDO's development of HOME-assisted units. Contracts are executed with each CHDO setting forth the maximum amount of CHDO funding to be provided, the time period in which the CHDO may submit for necessary and reasonable operating expenses and outlines the eligible expenses that the CHDO may submit for reimbursement. CHDO operating funds are provided only to CHDOs that are awarded and receive CHDO Reserve funds for development of HOME-assisted units in a particular program/fiscal year.

Other Matters

Finally, we request that all references to any specific applicant or HOME-assisted activity be removed from the Audit Report in favor of reference to activity numbers as is the case in the bulk of the Audit Report. In addition, we request that the Audit Reports reference to "questionable expenditures" be changed to "expenditures requiring additional support and/or documentation".

We appreciate any recommendations that could result in improvements to the State of Rhode Island HOME Investment Partnerships Program. All recommendations and findings listed in the Audit Report will be given serious consideration by Rhode Island Housing to improve our ability to better respond to the needs of low- and very low-income Rhode Islanders as we work to provide safe and decent housing opportunities.

Very truly yours,


Richard H. Godfrey, Jr.
Executive Director

Attachments

Comment 9

OIG Evaluation of Auditee Comments

- Comment 1 In response to recommendation 1A, while Rhode Island Housing officials agree that disbursements may not be made before a HOME agreement is executed, they believe that eligible expenses incurred before the execution of the HOME agreement are allowable. However, as noted in finding 1 of the report, section 5 of the Rhode Island Housing HOME agreements prohibits recipients from starting all or any part of the approved activity or incurring or becoming obligated with respect to any costs before the recipient's execution and delivery of the loan documents and notice to proceed. In each of the activities identified, expenses were incurred months or years before the HOME agreements were signed.
- Comment 2 In response to recommendation 1B, Rhode Island Housing officials contend that all expenses are eligible expenses within the definition of applicable HUD regulations and in no case were HOME funds disbursed for a particular item in excess of the HOME funds committed under the HOME agreement. We agree that the expenses are eligible HOME program expenses and HOME funds disbursed did not exceed the HOME funds committed under the HOME agreement. However, as noted in finding 1 of the report, section 5 of the HOME agreements provides that the recipient agrees to carry out the approved activity in accordance with the budget set forth in attachment A. Any amendments to this budget must be approved by Rhode Island Housing in writing before adoption. In the cases noted, budget amendments were not executed. Rhode Island Housing officials stated that they established a new policy of allowing payment for only those line item costs as budgeted in the HOME agreement. This policy change is responsive to our recommendation, but since we were not provided a copy during the audit, HUD should verify that the new policy is being followed during the audit resolution process.
- Comment 3 In response to recommendations 1C and 1D, Rhode Island Housing officials provided documentation showing that a deed restriction was executed and recorded in May 2014. We adjusted the report as necessary to indicate that a deed restriction is now in place. However, Rhode Island Housing officials did not provide support for \$1,839 associated with two drawdowns; therefore, those funds are still considered unsupported.
- Comment 4 In response to recommendation 1E, Rhode Island Housing officials stated that the residents did not overpay the applicant for their portion of the required rent because these tenants received Section 8 assistance. We revised the report to read, "As a result, overpayments of \$4,452 were made to the landlord by either the tenants or the Section 8 program." Rhode Island Housing stated that the applicant corrected its calculation of gross rent in 2013 to comply with the HOME agreement, deed restriction, and HOME regulations. However, for a year these two rents exceeded the maximum rent that could be charged. Therefore, during the audit resolution process, HUD should determine whether the tenants or the

Section 8 program overpaid rents and if so, require reimbursement to the affected party. Rhode Island Housing also agreed to provide additional guidance and assistance to an applicant or owners of developments that provide affordable homes for residents that participate in the Section 8 Housing Choice Voucher Program to ensure rent is within guidelines, and HUD should review this guidance during during the audit resolution process.

- Comment 5 In response to recommendation 1F, Rhode Island Housing officials believe that the application properly presented the acquisition cost because other costs were included in that figure, and they provided additional information on these costs. We reviewed the additional information and noted that costs such as insurance, taxes, and fencing were attributed to acquisition, but we do not agree that those costs should be classified as acquisition costs. However, Rhode Island Housing officials acknowledge that due to continued litigation, the project is unlikely to proceed any time soon and have agreed to deobligate the \$500,000 HOME award.
- Comment 6 In response to recommendations 1G and 1H, Rhode Island Housing officials stated that they will amend budgets as necessary for eligible expenditures if appropriate and stated that their staff conducts monitoring of HOME-assisted projects to ensure that owners and sponsors continue to comply with HOME agreements, deed restrictions, and Federal rules and regulations. These actions are responsive to our recommendations, and during the audit resolution process, HUD should verify that necessary budget amendments have been made.
- Comment 7 In response to recommendation 2A, Rhode Island Housing officials maintained that there was adequate supporting documentation in the three CHDO files referenced to justify the CHDO expenses; however, this support was not provided. The officials should provide the support to HUD for its review and determination during the audit resolution process.
- Comment 8 In response to recommendation 2B, Rhode Island Housing officials stated that they have established CHDO policies and procedures in accordance with regulations at 24 CFR 92.208. These actions are responsive to our recommendations, and HUD should review Rhode Island Housing's policies and procedures related to CHDO operations in the audit resolution process.
- Comment 9 OIG agreed with the request, and we made adjustments where applicable.

Appendix C

Schedule of Sampled HOME Units

	Activity number	HOME funds invested	Costs incurred before agreement	Costs not in budget	Costs exceed budget	Unsupported drawdowns	Excess rent charged tenants	Application not accurate	Unsupported	Ineligible	Funds to be put to better use
1	4511	\$940,000				X			\$1,839		
2	4996	\$500,000	X							\$400,000	
3	5023	\$260,000	X	X						\$44,759	
4	4760	\$300,000			X				\$109,516		
5	4338	\$119,018			X				\$56,935		
6	4775	Canceled									
7	5021	\$500,000						X			\$500,000
8	4592	\$500,000	X	X	X				\$62,426	\$388,749	
9	4503	\$142,052		X	X				\$39,601		
10	4596	\$80,000		X	X				\$80,000		
11	5000	\$140,000		X	X				\$139,138		
12	4320	\$675,000	X		X				\$412,093	\$49,584	
13	4757	\$148,000			X				\$10,802		
14	4615	\$126,820		X	X				\$11,540		
15	4594	\$94,820			X		X		\$39,112		
16	4827	\$97,500									
17	4528	\$25,000									
18	4520	\$160,000		X	X				\$37,546		
Total		\$4,808,334	4	7	11	1	1	1	\$1,000,548	\$883,092	\$500,000
Total questioned costs										\$2,383,640	