



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

June 25, 2015

MEMORANDUM NO:
2015-CH-0801

Memorandum

TO: Virginia M. Sardone
Director of Affordable Housing Programs, DG

//signed//

FROM: Kelly Anderson
Regional Inspector General for Audit, Chicago Region, 5AGA

SUBJECT: HUD's Office of Affordable Housing Programs Could Improve Its Oversight of Participating Jurisdictions' HOME Investment Partnerships Program-Funded Rental Housing Projects' Leases

INTRODUCTION

We reviewed the U.S. Department of Housing and Urban Development's (HUD) Office of Affordable Housing Programs' oversight of leases in HOME Investment Partnerships Program-funded rental housing projects. The review was part of the activities in our fiscal year 2015 annual audit plan. Our objective was to determine whether HUD's Office had adequate oversight of participating jurisdictions¹ to ensure that leases between rental projects' owners and households for Program-funded units did not include language prohibited by HUD's regulations.

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 HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the review.

¹ States and local governments that HUD designated to administer the Program.

METHODOLOGY AND SCOPE

We performed our review from February through May 2015 at HUD's Chicago regional office located at 77 West Jackson Boulevard, Chicago, IL. The review covered the period January 2011 through December 2014.

To accomplish our objective, we reviewed applicable requirements, HUD guidance, and data from HUD's Integrated Disbursement and Information System.² We also interviewed HUD's staff.

We relied in part on data in HUD's System. Although we did not perform a detailed assessment of the reliability of the data, we performed minimal levels of testing and found the data to be adequately reliable for our purposes.

At the start of our review, the Director of HUD's Office of Affordable Housing Programs acknowledged that the Office could do more to ensure that leases between rental housing projects' owners and households for Program-funded units do not include prohibited language. The Director agreed to implement additional procedures and controls to reduce the risk that leases would contain prohibited language. Therefore, we significantly reduced the scope of our review. We performed our review in accordance with generally accepted government auditing standards, except that we did not assess the effectiveness of internal controls. These facts do not affect the significance of the conditions identified in this memorandum. Further, we believe that the evidence obtained provides a reasonable basis for our results and conclusions based on our review objective.

We provided our discussion draft audit memorandum to the Director of HUD's Office of Affordable Housing Programs during the review. We asked the Director to provide written comments on the memorandum by June 15, 2015. The Director stated that she agreed with the results of the review and the recommendation, but chose not to provide formal written comments on the memorandum. She would provide corrective actions to address the recommendation through the management decision process.

BACKGROUND

Authorized under Title II of the Cranston-Gonzalez National Affordable Housing Act, as amended, the Program is funded to increase the supply of affordable standard rental housing; improve substandard housing for existing homeowners; assist new home buyers through acquisition, construction, and rehabilitation of housing; and provide tenant-based rental assistance.

HUD awarded nearly \$4.6 billion in Program funds to participating jurisdictions for Program years 2011 through 2014. Participating jurisdictions reported more than 7,000 rental housing projects with nearly 89,000 Program-funded units as complete in HUD's Integrated Disbursement and Information System from January 2011 through December 2014. The

² See appendix A of this memorandum for a more detailed list of the documentation we reviewed to accomplish our objective.

participating jurisdictions drew down more than \$4.5 billion in Program funds for the projects. The following table shows (1) the number of rental projects that participating jurisdictions reported as complete, (2) the number of Program-funded units associated with those projects, and (3) the amount of Program funds that the participating jurisdictions drew down for the projects, for each year from January 2011 through December 2014.

Year	Rental projects	Program units	Program funds drawn down
2011	1,867	23,304	\$1,084,655,715
2012	2,104	25,191	1,375,568,318
2013	1,586	20,716	985,016,707
2014	<u>1,571</u>	<u>19,334</u>	<u>1,094,079,389</u>
Totals	<u>7,128</u>	<u>88,545</u>	<u>\$4,539,320,129</u>

HUD’s Office of Affordable Housing Programs has oversight responsibility for the Program. It relied on the monitoring activities of HUD’s field Offices of Community Planning and Development to ensure that participating jurisdictions complied with HUD’s regulations concerning the language used in leases for Program-funded rental housing projects.

RESULTS OF REVIEW

HUD’s Office of Affordable Housing Programs could improve its oversight of participating jurisdictions to ensure that leases between rental housing projects’ owners and households for Program-funded units do not include language prohibited by HUD’s regulations.³

Through a previous audit of the City of Chicago, IL’s Program, we identified that leases between rental new construction projects’ owners and households for Program-funded units in two projects included language prohibited by HUD’s regulations and the City’s regulatory agreements with the owners. This weakness occurred because the City lacked adequate procedures and controls to ensure that the leases did not contain prohibited language.⁴ As a result, the City drew down nearly \$7.4 million in Program funds for the two projects in which the rights of 73 households were not protected (see finding 1 in Office of Inspector General audit report 2014-CH-1011, issued September 30, 2014).

The Director of HUD’s Office of Affordable Housing Programs read our audit report concerning the City’s Program and acknowledged that the issue of rental leases including language prohibited by HUD’s regulations was an issue that HUD’s field Offices of Community Planning

³ See appendix B of this memorandum for HUD’s regulations.

⁴ The assistant commissioner of the Monitoring and Compliance Division in the City’s Department of Planning and Development stated that although the City did not review projects’ standard leases before the projects were completed and units were leased, the Division’s staff should have reviewed the projects’ leases during the City’s required annual compliance monitoring. However, the staff did not review the leases because it assumed that the owners used leases that complied with HUD’s regulations and the regulatory agreements. Further, the Division’s long-term Program monitoring requirements and procedures required owners to submit leases for new households only and did not specify that the Division’s staff should review the leases for prohibited language.

and Development had identified a number of times over the years through monitoring reviews of other participating jurisdictions' Programs. For instance,

- HUD's San Juan Office of Community Planning and Development identified, through a July 2014 monitoring review of the Municipality of Arecibo, PR's Program, that the Municipality's model lease between rental projects' owners and households included all nine provisions prohibited by HUD's regulations at 24 CFR (Code of Federal Regulations) 92.253(b).
- HUD's Boston Office of Community Planning and Development identified, through an April 2014 monitoring review of the City of Brockton, MA's Program, that a lease for a project unit contained an inappropriate provision that allowed the project's owner to give the household no less than 14 days written notice to terminate the lease.
- HUD's Minneapolis Office of Community Planning and Development identified, through a May 2009 monitoring review of the City of Minneapolis, MN's Program, that a lease for a project unit contained a provision prohibited by HUD's regulations and an inappropriate provision that allowed the immediate eviction of a tenant. The Director of HUD's Minneapolis Office of Community Planning and Development's June 26, 2009, letter to the City's coordinator stated that on a number of occasions, the Office had advised its participating jurisdictions that this was a problem with many of the leases being used.

The Director said that the Office of Affordable Housing Programs issued guidance⁵ and provided training⁶ that informed participating jurisdictions and rental projects' owners that leases between the owners and households must not include language prohibited by HUD's regulations. For example, in 2009, HUD issued two guides—"Compliance in HOME Rental Projects: A Guide for Participating Jurisdictions" and "Compliance in HOME Rental Projects: A Guide for Property Owners"—to assist participating jurisdictions and rental projects' owners in complying with Program requirements. The guides included references to prohibited language and checklists to ensure that leases would not contain language prohibited by HUD's regulations.

Further, exhibit 7-7 of HUD's Community Planning and Development Monitoring Handbook 6509.2, REV-6, CHG-1, contains a step for HUD's field Offices of Community Planning and Development staff to determine whether leases between rental projects' owners and households for Program-funded units include language prohibited by HUD's regulations. However, the handbook does not contain a step for determining whether a participating jurisdiction reviews, as part of its monitoring process, leases between rental projects' owners and households for Program-funded units to determine whether the leases include language prohibited by HUD's regulations.

⁵ The guidance included HUD's "Building HOME: A Program Primer", dated March 2008; "Compliance in HOME Rental Projects: A Guide for Participating Jurisdictions" and "Compliance in HOME Rental Projects: A Guide for Property Owners", issued in 2009; and "Monitoring HOME" guidebook, dated September 2010.

⁶ The training included Program rental housing compliance certification and developing effective written agreements courses from October 2007 through November 2011. The courses were suspended due to the updating of 24 CFR Part 92.

The Director also acknowledged that HUD's Office of Affordable Housing Programs could do more to ensure that leases between rental housing projects' owners and households for Program-funded units do not include prohibited language and agreed to implement additional procedures and controls to reduce the risk that leases would contain prohibited language. The procedures and controls included

- Considering the development and required use of a lease addendum for Program-funded rental projects;⁷
- Revising 24 CFR Part 92 to include additional regulations concerning (1) the use of a lease addendum for rental projects; (2) written agreements between a participating jurisdiction and a for-profit or nonprofit owner, developer, or sponsor of a rental project including an additional provision regarding leases; and (3) participating jurisdictions reviewing and approving leases for rental projects, as applicable;
- Issuing a HOMEfires⁸ to reinforce HUD's regulations; and
- Revising exhibit 7-7 of HUD's Community Planning and Development Monitoring Handbook 6509.2, REV-6, CHG-1, to include a procedure for HUD's field Offices of Community Planning and Development staff to determine whether a participating jurisdiction is reviewing and approving leases for rental projects as required by the revisions in 24 CFR Part 92.

RECOMMENDATIONS

We recommend that the Director of HUD's Office of Affordable Housing Programs

- 1A. Implement adequate procedures and controls to ensure that leases between rental housing projects' owners and households for Program-funded units do not include language prohibited by HUD's regulations.

If the above recommendation is implemented, the rights of households in Program-funded rental projects should be better protected.

⁷ Requiring the use of a lease addendum may not be feasible due to the different State and local laws.

⁸ HOMEfires is the official policy newsletter for the Program that answers specific policy questions.

Appendix A

METHODOLOGY AND SCOPE – DETAILED LIST OF DOCUMENTATION REVIEWED

To accomplish our objective, we reviewed

- Applicable laws; HUD’s regulations at 24 CFR Part 92, “Building HOME: A Program Primer”, Community Planning and Development Monitoring Handbook 6509.2 REV-6, CHG-1, “Monitoring HOME” guidebook, “Compliance in HOME Rental Projects: A Guide for Participating Jurisdictions”, “Compliance in HOME Rental Projects: A Guide for Property Owners”, Program rental housing compliance certification training slides, and draft “Developing HOME Written Agreements: A Guide for Participating Jurisdictions and Housing Owners, Developers, and Sponsors”; HUD’s field Offices of Community Planning and Development’s monitoring review letters to participating jurisdictions from 2006 through 2014 as applicable; and Office of Inspector General audit reports 2008-CH-1010, issued June 11, 2008, and 2014-CH-1011, issued September 30, 2014.
- Data from HUD’s System for the Program-funded rental housing projects that participating jurisdictions reported as complete in HUD’s System from January 2011 through December 2014.

Appendix B

HUD'S REGULATIONS

Regulations at 24 CFR 92.253(b) state that a lease between an owner and a tenant of rental housing assisted with Program funds may not contain the following provisions in which the tenant agrees (1) to be sued, to admit guilt, or to a judgment in favor of the owner in a lawsuit brought in connection with a lease; (2) that the owner may take, hold, or sell personal property of household members without notice to the tenant and a court decision on the rights of the parties; (3) not hold the owner or the owner's agents legally responsible for any action or failure to act, whether intentional or negligent; (4) that the owner may institute a lawsuit without notice to the tenant; (5) that the owner may evict the tenant or household members without instituting a civil court proceeding in which the tenant has the opportunity to present a defense or before a court decision on the rights of the parties; (6) to waive any right to a trial by jury; (7) to waive the tenant's right to appeal or to otherwise challenge in court a court decision in connection with the lease; (8) to pay attorney's fees or other legal costs even if the tenant wins in a court proceeding by the owner against the tenant; and (9) to accept supportive services that are offered. Section 92.253(c) states that an owner may not terminate the tenancy or refuse to renew the lease of a tenant of rental housing assisted with Program funds, except for serious or repeated violation of the terms and conditions of the lease; for violation of applicable Federal, State, or local law; for completion of the tenancy period for transitional housing or failure to follow any required transitional housing supportive services plan; or for other good cause. Good cause does not include an increase in the tenant's income or refusal of the tenant to purchase the housing. To terminate or refuse to renew tenancy, the owner must serve written notice upon the tenant specifying the grounds for the action at least 30 days before the termination of tenancy.

Regulations at 24 CFR 92.504(a) state that a participating jurisdiction is responsible for managing the day-to-day operations of its Program, ensuring that Program funds are used in accordance with all Program requirements and written agreements, and taking appropriate action when performance problems arise. The use of subrecipients or contractors does not relieve the participating jurisdiction of this responsibility.