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| Issue Date July 31, 2009 |
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| Audit Report Number 2009-NY-1014 |
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TO: Joan K. Spilman, Director, Public Housing Division, 2CPH

FROM: *Edgar Moore*
Edgar Moore, Regional Inspector General for Audit, 2AGA

SUBJECT: The Lackawanna Municipal Housing Authority, Lackawanna, New York, Needs to Improve Controls and Operational Procedures regarding Its Capital Fund Program

HIGHLIGHTS

What We Audited and Why

We audited the Lackawanna Municipal Housing Authority's (Authority) administration of its capital fund program. We selected this auditee based on the fact that the Authority pledged its future capital fund appropriations, as part of the Capital Fund Financing Program, and incurred a \$4.25 million long-term liability to perform lead abatement and modernization work in 90 project units. The objectives of this audit were to determine whether the Authority disbursed capital funds and procured contracts in accordance with U.S. Department of Housing and Urban Development (HUD) requirements.

What We Found

The Authority disbursed capital funds for questionable expenditures. Specifically, the Authority had no basis for charging management improvement expenditures to its capital fund program, charged the same expenses for multiple capital fund drawdowns, and could not support the eligibility of charges for inspection costs, force account labor, and audit costs. As a result, it lacked assurance that \$195,046 in expenditures was necessary or reasonable.

The Authority did not follow HUD requirements, its own procurement policy, and New York State General Municipal Law when awarding contracts. Specifically, the Authority (1) accepted a sealed bid with a known mistake, (2) failed to properly procure competitive proposal contracts, (3) failed to properly execute a noncompetitive contract, and (4) failed to follow small purchase and sealed bid procedures when obtaining general contracting services. As a result, more than \$3 million in capital funds was used for questionable procurement expenditures, and the Authority lacked assurance that the services contracted for were provided as intended.

What We Recommend

We recommend that the Director of HUD's Buffalo Office of Public Housing instruct the Authority to (1) reimburse the capital fund program from nonfederal funds the \$7,535 in excess drawdowns and the more than \$2.6 million in costs associated with the lead abatement/modernization contract; (2) provide supporting documentation to justify the eligibility of \$676,301 in questionable capital fund expenditures or reimburse the program from nonfederal funds any amounts not supported; (3) seek legal advice on whether the lead abatement/modernization contract should be rescinded in the best interest of the Authority; and (4) review and if appropriate disapprove any future change orders associated with the lead abatement/modernization contract.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We discussed the results of our review during the audit, provided a copy of the draft report to Authority officials, and requested their comments on June 19, 2009. Authority officials generally agreed with the findings and provided their written comments during the exit conference held on June 29, 2009. The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Lackawanna Municipal Housing Authority (Authority) is a public corporation providing 491 low-rent housing units at three housing projects located in Lackawanna, New York. The Authority received capital fund program formula grant subsidies from the U.S. Department of Housing and Urban Development (HUD) in 2007 and 2008 of \$1.1 million and \$1.2 million, respectively. It also received an operating subsidy of more than \$1.8 million in 2007 and approximately \$1.4 million in 2008. The Authority has been allocated an additional \$1.5 million in capital funds under the American Recovery and Reinvestment Act of 2009.

In September 2006, the Authority incurred a \$4.25 million long-term liability as part of the Capital Fund Financing Program to perform lead abatement and modernization work in 90 units in one of its projects. HUD regulations allow housing authorities to participate in this financing element of the capital fund program. Under the program, HUD recognizes that some authorities may not have enough funds in a single year to make all of the improvements necessary to adequately maintain their public housing. It allows an authority to borrow private capital to make improvements and pledge, subject to the availability of appropriations, a portion of its future-year annual capital funds to make debt service payments for either a bond or conventional bank loan transaction. The Authority's semiannual interest payments have already begun, and annual principal payments are to commence in September 2009. Both payments offset capital fund program grants.

Based on its last Public Housing Assessment System score, the Authority was found to be substandard physical; thus, it is subjected to HUD's extended oversight. The Real Estate Assessment Center performed two physical assessments for fiscal year 2007. For the inspection performed in February 2008, the Authority received a Physical Assessment Subsystem score of 17 and failed the reinspection in July 2008 with a score of 15. As a result, HUD's Recovery and Prevention Corps is planning a comprehensive review of the Authority's operations scheduled for June 2009.

The objectives of this audit were to determine whether the Authority disbursed capital funds and procured contracts in accordance with HUD requirements.

RESULTS OF AUDIT

Finding 1: The Authority Charged Questionable Expenditures to Its Capital Fund Program

The Authority disbursed capital funds for questionable expenditures. Specifically, the Authority failed to prepare a management needs assessment; charged the same expenses for multiple capital fund drawdowns; and could not support the eligibility of charges for inspection costs, force account labor, and audit costs. As a result, it lacked assurance that \$195,046 in expenditures was necessary or reasonable. We attribute these deficiencies to the Authority's failure to establish and implement accounting controls over disbursements that were sufficient to ensure compliance with applicable regulations.

Failed to Prepare a Management Needs Assessment

The Authority had no basis for charging management improvement expenditures to its capital fund program grants since it failed to prepare a management needs assessment. Regulations at 24 CFR [*Code of Federal Regulations*] 968.315(e) provide that a comprehensive plan shall identify all of the physical and management improvements needed for an authority. The plan should include a comprehensive assessment of the improvements needed to upgrade the management and operations of the authority so that decent, safe, and sanitary living conditions will be provided.

The management needs assessment should include an identification of the most current needs. Items identified should include management, financial, and accounting control systems of the authority; the adequacy and qualifications of personnel employed by the Authority in its management and operations; and the adequacy and efficacy of resident programs and services. In addition, the management needs assessment should include a preliminary cost estimate for addressing all the needs identified without regard to the availability of funds.

The Authority was unable to provide us with such an assessment. Thus, it did not have the framework for charging management improvement expenditures to its capital fund program.

The Authority charged \$127,137 in management improvements to its 2005, 2006, and 2007 capital fund program grants from the sample expenditures reviewed. The expenditures represented costs pertaining to the salary and expenses of a recreational leader, resident activities, and nonresident services. The Authority was unable to provide sufficient documentation to support that the charges met

the eligibility requirements for management improvements. Since the Authority failed to prepare a management needs assessment and was unable to provide evidence that the charges were allowable, we consider the \$127,137 in management improvement charges to the program to be unsupported pending an eligibility determination by HUD.

Charged the Same Expenses to Support Multiple Drawdowns

The Authority charged the same expenses to support multiple drawdowns to the capital fund program. A review of capital fund drawdowns during the period July 2005 through June 2008 disclosed six excess drawdowns totaling \$7,535. For example, an invoice in the amount of \$3,850, dated September 21, 2007, for electrical work was charged to a capital fund drawdown on February 29 and May 13, 2008. Regulations at 24 CFR 85.20 require that fiscal control and accounting procedures be sufficient to permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes. Auditee officials acknowledged that their accounting procedures at the time made them susceptible to weaknesses in this area. We attribute the multiple drawdowns to inadequate accounting controls. Accordingly, we consider the disbursement of \$7,535 in capital funds to be ineligible.

Eligibility of Expenditures Not Supported

The Authority charged \$60,374 in expenditures to the capital fund program that were not supported. For the sample of capital fund drawdowns reviewed, the Authority did not provide adequate support that inspection costs, force account labor costs, and audit costs were eligible. For example, the Authority charged \$38,998 for the total salary of the clerk of the works to architectural/engineering and consultant fees. The supplement to HUD Handbook 7475.1 provides that construction supervisory and inspection costs incurred during construction are considered front-line costs. For those authorities that use their own personnel to carry out this function, a time sheet will be required to substantiate the construction supervisor's time. Only actual documented costs pertaining to construction supervision activities, such as inspections incurred during the construction phase, can be charged directly. However, the Authority did not maintain time sheets to substantiate the clerk of the works' time.

In addition, the Authority charged \$18,961 in force account labor to its capital fund program without adequate support. The support did not provide that the costs were reasonable or eligible to be charged to the program. For example, in relation to ineligible costs, the support provided, such as contractor cost estimates

and timesheets of the Authority's maintenance staff, did not distinguish whether the costs were for routine maintenance or capital improvements. OMB [Office of Management and Budget] Circular A-87 defines reasonable cost as cost that does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost.

Also, the Authority charged \$2,415 for auditing services that did not relate directly to capital fund program grant audits but, instead, related to routine operational accounting services. Regulations at 24 CFR 968.112(k) provide that eligible costs are limited to the portion of the audit costs that are attributable to the modernization program.

Conclusion

The Authority did not establish and implement adequate accounting controls to ensure that capital fund expenditures complied with applicable regulations. As a result, \$195,046 in questioned costs was charged to the capital fund program without assurance that the costs were necessary and reasonable. We attribute these deficiencies to the Authority's failure to establish and implement accounting controls over disbursements that were sufficient to ensure compliance with applicable regulations.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Public Housing instruct the Authority to

- 1A. Provide documentation to justify the \$127,137 in management improvement expenditures so that HUD can make an eligibility determination. Any unsupported costs determined to be ineligible should be reimbursed to the capital fund program from nonfederal funds.
- 1B. Prepare and maintain a management needs assessment identifying the Authority's most current needs including but not limited to management, financial and accounting control systems of the Authority, and the adequacy and efficacy of resident programs and services. The management needs assessment should include a cost estimate for addressing all identified needs without regard to the availability of funds.
- 1C. Identify in its annual statements and performance and evaluation reports management improvement expenditures in relation to the Authority's needs assessed so that HUD can make a determination of eligibility.

- 1D. Reimburse the capital fund program from nonfederal funds the \$7,535 in excess drawdowns pertaining to electrical work, accounting services, and tenant employment and recreational activities.
- 1E. Establish and implement written accounting procedures that address the roles and responsibilities of accounting staff, including performing monthly reconciliation of capital funds and reviewing drawdown requests to ensure compliance with applicable program regulations.
- 1F. Provide documentation to justify the \$60,374 in inspection costs, force account labor, and audit costs charged to the program so that HUD can make an eligibility determination. Any unsupported costs determined to be ineligible should be reimbursed to the capital fund program from nonfederal funds.
- 1G. Provide continuing education to ensure that all Authority staff and board members involved with the capital fund program grants are familiar with laws and regulations, thus strengthening the controls to ensure that only eligible and supported costs are charged to the capital fund program grants.

Finding 2: The Authority Improperly Procured Contracts and Professional Services

The Authority did not follow HUD requirements, its own procurement policy, and New York State General Municipal Law when awarding contracts. Specifically, the Authority (a) accepted a sealed bid with a known mistake, (b) failed to properly procure competitive proposal contracts, (c) failed to properly execute a noncompetitive contract, and (d) failed to follow small purchase and sealed bid procedures when obtaining general contracting services. As a result, more than \$3 million in capital funds was used for questionable procurement expenditures, and the Authority lacked assurance that the services contracted for were provided as intended. We attribute these deficiencies to the Authority's not establishing operational procedures to implement its procurement policy to ensure compliance with applicable regulations.

Sealed Bid Accepted with Known Mistake

As part of HUD's Capital Funds Financing Program, the Authority received \$4.25 million in bond proceeds for lead-based paint abatement and modernization of 90 units at one of its projects. Review of the Authority's contract award and administration process determined that the Authority accepted a sealed bid for the lead abatement/modernization work with a known mistake pertaining to \$400,000 in additional plumbing work. Specifically, the contractor did not include the cost of installing toilets, sinks, tubs, faucets, cleaning drains, and other plumbing-related work in its bid for work pertaining to the lead abatement/modernization project. Although the mistake was acknowledged by the contractor in correspondence with the architect/engineer and officials for the project, the Authority did not follow New York State General Municipal Law when awarding the lead abatement/modernization contract.

Section 103 of the New York State General Municipal Law requires the withdrawal and rebid of bids containing mistakes; however, the Authority accepted the bid and awarded the \$3.4 million contract. Rather than withdrawing the bid and initiating the bid process again, the Authority opted arbitrarily to go against the advice of its own legal counsel and awarded the bid containing the mistake. In doing so, it inappropriately restricted competition.

At the time of this report, the Authority had paid more than \$2.2 million for the contracted abatement/modernization work. In addition, it did not maintain documentation, including cost analyses, to justify \$406,324 in change orders to the contract. The Authority had increased the original contract amount by approximately 13 percent and significantly modified the scope of services to be provided, which may have been an attempt for the contractor to compensate for the

bid mistake. Accordingly, we consider the use of more than \$2.6 million in capital funds to be ineligible. Further, the Authority should be prohibited from using program funds for the remaining contract balance of nearly \$1.2 million for unfinished work, \$26,686 for unfinished change order work, and \$532,262 for projected future change orders, thereby realizing a total cost savings of more than \$1.7 million. The Authority should be instructed to seek legal advice on whether the contract should be rescinded.

Improper Procurement of Competitive Proposal Contracts

The Authority failed to properly procure a competitive proposal contract for architectural/engineering work. It did not provide evidence to support the reasonableness of an architectural and engineering contract and failed to administer the terms of the contract totaling \$227,260. Contrary to regulations at 24 CFR 85.36, the Authority failed to maintain records sufficient to detail the significant history of the procurement action. Specifically, the Authority did not perform a cost analysis, which is required when the elements of estimated cost are part of the evaluation to select the service contract. In addition, the Authority was not able to provide evidence of a negotiation of price. Its procurement policy provides that negotiations shall be conducted with offerors who submit proposals determined to have a reasonable chance of being selected for award. There was a large discrepancy between the proposed fee and the awarded fee.

Also, the Authority did not properly execute the terms of the contract. Specifically the Authority did not (1) define the scope of work in writing and request that the architect provide a detailed cost breakdown to perform the work, (2) perform a cost analysis to document the cost reasonableness of the architectural and engineering cost breakdown, (3) develop a finding of fact to document the rationale for award of the work, (4) issue purchase orders for most of the work, (5) ensure that something of value would be received for the services paid, and/or (6) pay the vendor based on the terms of the contract. The lack of a defined written scope of services to be performed prevented the Authority from determining whether the contractor performed according to the Authority's intentions. Further, the Authority was unable to determine whether the most economical approach was used in procuring the services since it did not perform an analysis of the cost reasonableness. Consequently, we consider the use of \$227,260 in capital funds to be unsupported pending a HUD eligibility determination.

In addition, the Authority failed to properly procure a competitive proposal contract for auditing services. Contrary to regulations at 24 CFR 85.36, the Authority did not advertise for the auditing services and did not identify the relative value of the evaluation factors. Thus, the Authority's evaluation and award process appeared to preclude open and free competition. When

professional services can be obtained by competitive conditions, proposals should be obtained from an adequate number of qualified sources to permit open and free competition and to ensure that adequate information is available to evaluate significant factors, such as the price of the contract and the contractor's ability to perform the services. Accordingly, we consider the use of \$1,500 in capital funds for auditing services to be unsupported pending a HUD eligibility determination.

Improper Execution of Noncompetitive Proposal Contract

The Authority failed to properly execute a noncompetitive contract for accounting services performed during 2006 through 2007. By not executing a contract, the Authority did not obtain a legally binding document that would protect it against nonperformance by the accounting firm. Further, failure to execute a contract precluded the Authority from identifying the actual services expected to be completed. Although the Authority executed a contract in 2008 with the same firm, it did not maintain evidence to support the basis of sole source contracting. In 2008, the Authority failed to meet the requirements for procuring noncompetitive contracts in accordance with its own procurement policy and regulations at 24 CFR 85.36, which require written documentation to justify the Authority's rationale for its method of procurement and that cost analyses be performed. As a result, we consider the use of \$32,929 in capital funds for accounting services to be unsupported pending a HUD eligibility determination.

Failure to Follow Small Purchase and Sealed Bid Procedures

The Authority failed to follow the procedures for small purchases and sealed bidding when procuring general contracting work. Although the Authority remained within its small purchase procurement policy threshold limitation of \$50,000 for eight payments made to a general contractor, it did not obtain price or rate quotations from three qualified sources for five payments totaling \$30,550 in accordance with 24 CFR 85.36. In addition, it appeared that the Authority circumvented the appropriate procurement process when procuring roofing work. Specifically, the Authority paid \$71,190 under three invoices for the same scope of work performed during July 2007. The inclusion of identical work under three invoices raises the question as to whether the sealed bid process was circumvented by splitting the work within the confines of the small purchase threshold limitations. Accordingly, we consider the use of \$101,740 in capital funds for general contracting work as unsupported pending an eligibility determination by HUD.

In addition, the Authority did not maintain adequate procurement documentation to support the solicitation of bids or its method of bid solicitation for \$125,361 in appliance purchases contrary to 24 CFR 85.36. Further, contrary to requirements in HUD Handbook 7460.8, the Authority failed to enter into a contract for the recurring appliance purchases. As a result, we consider the \$125,361 in appliances purchases as unsupported costs pending an eligibility determination by HUD.

Conclusion

The Authority had not established the operational procedures to implement its procurement policy to ensure compliance with all applicable regulations. As a result, it lacked assurance that more than \$3 million in capital fund expenditures was necessary or reasonable and that the services contracted for were provided as intended. This lack of oversight by the Authority to ensure that capital fund contracts were awarded in a prompt, fair, and reasonable manner is a major concern in light of the Authority's having received an additional \$1.5 million in capital funds under the American Recovery and Reinvestment Act of 2009. Thus, the Authority should seek legal advice on whether the lead abatement / modernization contract should be rescinded, and review and disapprove any future change orders related to this contract, thus resulting in a realized program cost savings.

Recommendations

We recommend that the Director of HUD's Buffalo Office of Public Housing instruct the Authority to

- 2A. Reimburse the capital fund program from nonfederal funds for the \$2,608,258 in ineligible lead abatement/modernization contract costs.
- 2B. Seek legal advice on whether the lead abatement/ modernization contract should be rescinded in the best interest of the Authority, thus resulting in a cost savings of \$1,224,652 for the remaining contract balance.
- 2C. Review and if appropriate disapprove any future change orders associated with the lead abatement/modernization contract. By rejecting the future change orders, a projected cost savings of \$532,262 will be realized.
- 2D. Provide documentation to justify the \$488,790 in unsupported contract costs (\$227,260 for architectural/engineering services, \$1,500 for audit services, \$32,929 for accounting services, \$101,740 for general contracting work, and \$125,361 for appliance purchases) so that HUD can make an eligibility determination. Any unsupported costs determined to

be ineligible should be reimbursed from nonfederal funds. If the accounting services are determined to be ineligible, HUD should instruct the Authority to terminate the contract.

SCOPE AND METHODOLOGY

Our review focused on whether the Authority disbursed capital funds and procured contracts in accordance with HUD requirements. To accomplish our audit objectives, we reviewed relevant HUD regulations, program requirements, and applicable laws. In addition, we analyzed the Authority's obligation and disbursement of capital funds in HUD's Line of Credit Control System. We reviewed HUD's administrative files and monitoring reports for the Authority's capital fund program. We conducted interviews with the Authority's staff to gain an understanding of the internal controls related to the administration of the capital fund program. We also reviewed the Authority's program policies and procedures, five-year and annual plan, annual audited financial statements, board of commissioners minutes, budgets, general ledgers, and Line of Credit Control System drawdown vouchers related to the capital fund program.

For fiscal years 2006 through 2008, we selected a nonstatistical sample of six contracts to perform a thorough review of procurement documentation including the award process and administration. For the periods June 2006 through August 2006 and December 2007 through February 2008, we selected a nonstatistical sample of 20 capital fund drawdowns totaling \$863,520 and representing about 28 percent of the Authority's capital fund program to review the eligibility and support of the expenditures.

The review covered the period July 2005 through June 2008 and was extended as necessary. We performed audit work from October 2008 through May 2009 at the Authority's office located at 135 Odell Street, Lackawanna, New York.

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

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following controls are achieved:

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. They include the processes and procedures for planning, organizing, directing, and controlling program operations, as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.
- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

Based on our review, we believe that the following item is a significant weakness:

- The Authority did not have adequate controls over its program operations and compliance with laws and regulations when it did not establish adequate accounting controls to ensure that costs charged to the capital fund program were eligible and when it did not establish operational procedures for implementing its procurement policy to ensure compliance with applicable regulations and HUD program requirements (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 | | \$127,137 | |
| 1D | \$7,535 | | |
| 1F | | \$60,374 | |
| 2A | \$2,608,258 | | |
| 2B | | | \$1,224,652 |
| 2C | | | \$532,262 |
| 2D | | \$488,790 | |
| Total | \$2,615,793 | \$676,301 | \$1,756,914 |

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. If the Authority implements our recommendations for rescinding the lead abatement/modernization contract and disallowing any future change orders associated with the contract, it will ensure a cost savings to its capital fund program.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

lackawanna
municipal
housing
authority

July 13, 2009

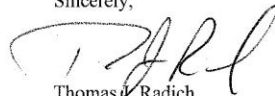
Edgar Moore
Regional Inspector General for Audit
U.S. Dept of Housing and Urban Development
26 Federal Plaza, Rm. 3430
New York, N.Y. 10278

Dear Mr. Moore,

The Lackawanna Municipal Housing Authority has reviewed the U.S. Department of Housing and Urban Development Office of Inspector General Draft Audit Reports that were submitted to us on June 11, 2009, and June 19, 2009.

The attached documents present LMHA management's responses to the two draft audit reports.

Sincerely,



Thomas V. Radich
Executive Director

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

LACKAWANNA MUNICIPAL HOUSING AUTHORITY

Comments on Draft Audit Report dated June 19, 2009
of the Office of Inspector General
of U.S. Department of Housing and Urban Development

July 13, 2009

The Lackawanna Municipal Housing Authority (the "Authority") offers the following comments on the Draft Audit Report (the "Draft Audit") prepared by the Office of Inspector General ("OIG") of the U.S. Department of Housing and Urban Development ("HUD") which was delivered to the Authority by letter dated June 19, 2009, from Edgar Moore, Regional Inspector General for Audit.

Comment 1

Comment 1. Alleged Failure to Prepare Management Needs Assessment. On pages 5 and 6, the Draft Audit questions the eligibility as "management improvements" of \$127,137 in expenses for a recreational leader, resident activities and nonresident services due to the Authority's alleged failure to prepare a management needs assessment. Notwithstanding that the Authority had not recently updated its Management Needs Assessment, the Authority is confident that upon a review by HUD, all such expenses will be found to constitute legitimate management improvement expenses. Budgets reflecting the salaries and other expenses in question were submitted to and approved by the regional HUD office for each of the years covered by the Draft Audit with no request from HUD for an updated Management Needs Assessment.

Comment 2

Comment 2. Alleged Charge of Same Expenses to Support Multiple Drawdowns. On page 6, the Audit Report alleges that six drawdowns totaling \$7,535 were charged twice against the capital fund program. The Authority acknowledges that clerical errors were made, but those errors were subsequently corrected and the Authority did NOT draw funds for the same expenses more than once.

Comment 3

Comment 3. Support of Expenditures. On page 6, the Draft Audit questions the expenditure of capital funds toward the salary of an Authority employee who served as a clerk of the works for the Authority's construction project. The Authority believes that the allocation of the employee's time to such activities was appropriate and notes that such expenditures were approved by HUD.

Comment 4

Similarly, on pages 6 and 7, the Draft Audit questions the allocation of \$18,961 in force account labor to the capital fund program. The expense constituted overtime required for painting and patch work which the Authority believes was properly categorized as capital improvements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 5

On page 7, the Draft Audit questions the charge of \$2,415 for auditing services to the capital fund. Although the Authority believes that such allocation of auditing fees was appropriate, it acknowledges that it lacks adequate documentation to demonstrate that.

Comment 6

Comment 4. Sealed Bid. On pages 9 and 10, the Draft Audit alleges that the Authority accepted a sealed bid for work relating to lead-based paint abatement and modernization of 90 units in violation of New York law and the advice of its own counsel. This allegation is incorrect. The Authority's counsel advised that the Authority could permit the contractor to withdraw its bid due to the mistake and could rebid the project, but could not modify the bid to correct the mistake. Since the successful bidder was willing to stand by its original bid, without modification, the Authority had the right under the law to accept that bid, which it did.

Comment 7

The Audit Report suggests that change orders that have been approved in connection with the lead abatement and renovation project "may have been an attempt for the contractor to compensate for the bid mistake." It bases that suggestion on the Authority's alleged failure to "maintain documentation, including costs analyses, to justify" the change orders. In fact, the change orders all pertain to additional work discovered during the renovation process, and the required documentation, which was not requested by the HUD auditors prior to the Authority's exit interview, is in the possession of the Authority's architectural and engineering firm. All change orders were reviewed and approved by the architectural and engineering firm prior to submission to the Authority for its approval.

Comment 8

The Audit Report recommends that the Authority seek legal advice as to whether the lead abatement/renovation contract can be rescinded, which the Audit Report indicates would result in cost savings of more than \$1.7 million. Aside from the cost of obtaining such a legal opinion and of the litigation that would likely ensue from any attempt to rescind the contract, this suggestion ignores the fact that the lead abatement and renovation work would have to be completed by someone. There can be no assurance that bids to complete the work would be less than the remaining cost of the existing contract, but they certainly would not result in avoiding the entire remaining cost.

Comment 9

Comment 5. Procurement of Competitive Proposal Contracts. On page 10, the Draft Audit criticizes the payment of \$227,260 to the Authority's architectural and engineering firm. The Authority procured its first blanket A&E contract per HUD's suggestion and recommendation. Our procurement policy was generally followed but agrees and acknowledges that as a first time endeavor it was lax on some of the said policy and will meet with the Buffalo HUD office to seek advice on how to revise and administer this policy more efficiently in the future.

Comment 10

On pages 10 and 11, the Draft Audit also criticizes the procurement of a competitive proposal for auditing services for \$1,500 due to the Authority's failure to advertise for the auditing services. The Authority acknowledges that it may not have complied strictly with the procurement regulations with respect to this auditing contract and will endeavor to be more diligent in the future.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 10

Comment 6. Execution of Noncompetitive Proposal Contract. On page 11, the Draft Audit criticizes payments by the Authority to a provider of accounting services. The Authority acknowledges the need to follow more strictly the procurement regulations relating to noncompetitive proposals unless it determines that there are a sufficient number of qualified providers of the required services to permit a competitive request for proposals.

Comment 11

Comment 7. Small Purchase and Sealed Bid Procedures. On page 11, the Draft Audit criticizes a total of five payments totaling \$30,550 as not having been made in compliance with procurement policies. One of the five payments represented payment of an invoice that covered several flooring jobs, each of which was under \$2,000, and each of which arose in the context of turning a residential unit over to a new tenant. Therefore, the Authority does not believe those jobs required multiple quotations. A second payment represented required code compliance work discovered in the process of doing repair work resulting from a fire. Such payment was covered by insurance proceeds and therefore did not involve federal funds. The remaining three payments were each for emergency repairs, which the Authority understands permits noncompetitive proposals so as to avoid delays in providing such repairs.

Comment 12

On page 11, the Draft Audit criticizes the payment by the Authority of \$71,109 under three invoices for the same scope of work, suggesting this was a means to stay within the small purchase threshold limitations. In fact, the work involved repair of four roofs. Initially, emergency work was required on two roofs as a result of damage suffered during a wind and hail storm. The Authority procured such work on an emergency basis. Subsequently, the Authority requested quotations for the repair of two additional roofs on a non-emergency basis, as a result of which the same contractor was awarded the work. Although awarded to the same contractor, the jobs were not part of the same contract.

The Lackawanna Municipal Housing Authority has been a model agency for the past 8 years. In 2001, when I was appointed Director, this agency was supplying affordable housing, period, no extras, and no programs. There weren't any opportunities or added services for the tenants.

Since that time this Authority has expanded to a high performing agency with many cost cutting measures and extra services offered to our tenants. We have accomplished so much in such a short period of time.

Our **RESOURCE CENTER**, (HUD recommended) thru a \$ 300,000 Neighborhood Networks grant that was applied for by this administration and approved is up and running and assisting our tenants both young and old in there quest for a better life thru many different programs and services.

Our **WELLNESS CENTER** (HUD recommended) is a full workout facility at the disposal to our residents to help in their goal of desired physical fitness.

These two buildings were vacant, unused, and labeled as storage areas in 2001.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

The **ENERGY PERFORMANCE CONTRACT** (HUD recommended) which we are about to break ground on was another project which we were not required to perform. Once again, very time consuming and taxing to see to the end.

Our **CFPP PROJECT** (HUD recommended) is 60% complete. The hours of work it took to see this program become a reality were exorbitant and very challenging. This project when completed in 2010 will render the final 90 units lead free and render the Lackawanna Housing Authority completely lead free and modernized.

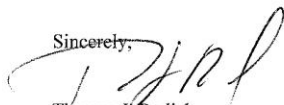
These projects and programs are not required as part of our daily duties. They are going above and beyond. The Buffalo HUD office, our mentor, or overseer surely should realize that fact.

Aside from all the extra work and required reporting and monitoring that comes with extra projects, improvements and initiatives comes the day to day work that a skimpy management staff has to address. This work is never ending and perpetual and very unrewarding to say the least.

With that being said, this agency will continue to move forward and make this neighborhood a better place to live for our residents as we have since 2001.

The Buffalo office surely realizes that our Authority has worked diligently and has come a long way in becoming an integral part of this community and deserves some type of intervention or assistance in this matter. We are assisting our neediest residents on a daily basis not only to provide basic shelter but also to provide a better quality of life and the pursuit of self sufficiency and to realize the most cherished sentiment of all mankind, self respect.

Sincerely,



Thomas J. Radich
Lackawanna Housing Authority
Executive Director

OIG Evaluation of Auditee Comments

- Comment 1** Officials for the Authority agree that an updated management needs assessment was not prepared, but contend that HUD’s Regional Office approved the budget each year reflecting the salaries and other expenses with no request for an updated management needs assessment. HUD’s approval of the budget would be based on the assumption that the items in the budget were in agreement with the management needs assessment. Since an amendment to the comprehensive annual plan, which includes the management needs assessment, was not submitted by the Authority, HUD would not have been aware that the items in question (that may have been in the budget) were not in the management needs assessment. The Authority is required to maintain an updated management needs assessment on-site and have it available for HUD review. Nevertheless, the Authority could not provide a management needs assessment that identified the items in question during the review.
- Comment 2** Officials for the Authority agree that clerical errors were made, but state that the errors were subsequently corrected and the Authority did not draw funds for the same expenses more than once. We were not provided with evidence that all of the multiple drawdown errors were subsequently corrected. However, capital funds were indeed drawn for the same expenses more than once. As such, the \$7,535 is still questioned.
- Comment 3** Officials for the Authority state that the allocation of the clerk of the works’ time was appropriate and the expenses were approved by HUD. Although the HUD approved annual plan included a sub-item called inspection services in the “Fees and Costs” budget line item, to which this employee’s salary was charged, the Authority has not maintained time sheets to substantiate that the clerk of the works’ time pertained only to construction supervisory activities, such as inspections, to warrant being allocated to the capital fund program.
- Comment 4** Officials for the Authority contend that the \$18,961 in force account labor charged to the program, consisting of overtime costs for unit painting and patch work, represents properly categorized capital improvements. HUD Handbook 7485.3 G permits the use of capital funds for force account labor to perform modernization activities. However, the support provided was not adequate to determine whether the clean up and painting of vacated units is a normal operating activity or a capital improvement, thus, the \$18,961 charged to the program is considered unsupported.
- Comment 5** Officials for the Authority agree that the \$2,415 for auditing services charged to the capital fund lacks adequate supporting documentation. Thus, the Authority needs to provide supporting documentation to justify the auditing services to HUD during the audit resolution process so that HUD can determine its eligibility.

- Comment 6** Officials for the Authority state that the Authority’s counsel advised that they could permit the contractor to withdraw its bid and then rebid the lead-based paint and modernization project, but they could not modify the bid to correct the plumbing mistake. Officials contend that since the successful bidder was willing to stand by its original bid, without modification, the authority had the right under law to accept that bid. Regardless of the officials interpretation of its legal counsel’s advice, the opinion issued by its counsel and Section 103 of New York State General Municipal Law require the withdrawal and re-bid of proposals containing mistakes.
- Comment 7** Officials for the Authority contend that the change order documentation, which was reviewed, approved and maintained by its architectural/engineering firm, was not requested by the auditors. However, in response to repeated requests, Authority officials failed to provide the documentation to support the cost reasonableness of the change orders. The absence of these documents was discussed during our review, at the end of our onsite fieldwork, and at the exit conference. Further, it should be noted that in accordance with HUD regulations, the Authority’s contract officer, and not the architectural/engineering firm, is responsible for reviewing and approving change order documentation, including cost analyses. Nevertheless, if any additional documentation exists it should be submitted to HUD’s field office officials for review during the audit resolution process.
- Comment 8** Officials for the Authority question the \$1.7 million in cost savings contending that aside from the cost of obtaining a legal opinion resulting in possible litigation, the lead abatement and renovation work would still have to be completed by another contractor. The fact remains that, contrary to New York State Law, the Authority awarded the contract with a known bid mistake and in doing so, inappropriately restricted competition. The best course of action going forward is for the Authority is to seek legal advice to determine the appropriate remedy for the remaining contracted work. While we acknowledge that the Authority will incur costs to complete the lead abatement and modernization work, if a legal opinion indicates that the current contract should cease, a new contract competitively bid may reduce the costs.
- Comment 9** Officials for the Authority agree that the contract with the Authority’s architectural and engineering firm was not procured in accordance with its own procurement policy. Officials intend to seek advice from HUD on how to revise and administer their procurement policy more efficiently in the future. As such, the Authority needs to maintain records sufficient to detail the significant history of future procurement actions, and provide supporting documentation to justify the unsupported costs to HUD during the audit resolution process.
- Comment 10** Officials for the Authority agree that the contract for auditing and accounting services was not procured in accordance with procurement regulations. As such, officials acknowledge the need to comply with procurement regulations

pertaining to competitive and noncompetitive proposals, and agree to be more diligent in the future. Thus, Authority officials need to provide documentation to support that the costs for the auditing and accounting services are eligible to HUD during the audit resolution process.

Comment 11 Officials for the Authority state that one of the five questioned payments totaling \$30,550 represented payment of an invoice that covered several flooring jobs, each of which was under \$2,000 and pertained to unit turn over. Officials contend that the second payment, representing required code compliance work discovered in the process of performing repairs resulting from a fire, was covered by insurance proceeds and did not involve federal funds. The three remaining payments were for emergency repairs. However, no supporting documentation pertaining to the flooring jobs, code compliance work, and the emergency repairs was provided. Further, all five payments were made with capital funds. Thus, we consider the \$30,550 as unsupported pending an eligibility determination by HUD.

Comment 12 Officials for the Authority state that the roof repairs for two of the roofs included in the \$71,109 contractor payment were for emergency repairs and two were for non-emergency repairs. However, a review of the supporting documentation suggests that the same repair work was conducted on the four roofs simultaneously. Thus, the officials should have procured the roof repair work under one sealed bid process. In addition, there was no documentation provided to support the use of non-competitive proposal contract procurement for the emergency repairs.