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| Issue Date July 20, 2009 |
| Audit Report Number 2009-AT-1009 |

TO: Ada Holloway, Director, Office of Public Housing, 4APH

//signed//

FROM: James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: The Housing Authority of the City of Newnan, Georgia, Inappropriately Encumbered Assets and Advanced Funds to Support Its Nonprofit Organization

HIGHLIGHTS

What We Audited and Why

We audited the Housing Authority of the City of Newnan's (Authority) activities with its related nonprofit organization, the Newnan Housing Development Corporation. The review was performed based on concerns that the Authority encumbered its assets, used its federal funds to support nonprofit development activities, and had a conflict-of-interest transaction. Our objective was to determine whether the Authority inappropriately used funds and assets restricted by its annual contributions contract with the U. S. Department of Housing and Urban Development (HUD) to support the operations of its nonprofit organization and incurred costs for insurance that involved a conflict of interest.

What We Found

The Authority inappropriately encumbered \$649,976 in HUD-restricted funds in violation of its contract with HUD and also violated an agreement it made with HUD concerning the sale and disposition of Authority property. The Authority used the \$649,976 to open a certificate of deposit account as collateral to secure a bond issuance on behalf of its nonprofit organization. As of December 31, 2008, the certificate of deposit account balance was \$673,859. In addition, the

Authority encumbered its assets as collateral for a \$150,000 loan on behalf of the nonprofit organization. These encumbrances occurred because the Authority lacked the controls necessary to avoid encumbrances. As a result, the encumbrances put the Authority's funds at risk.

The Authority inappropriately used \$221,531 of its public housing program funds for nonfederal development activities in violation of its annual contributions contract with HUD. In addition, it inappropriately used HUD funds to make 31 monthly payments on a \$150,000 loan on behalf of its nonprofit organization. This condition occurred because the Authority's board of commissioners did not establish sufficient controls to ensure that the executive director followed terms and conditions established in the contract. Also, the nonprofit organization was not financially sound, and the Authority did not have an updated comprehensive marketing strategy to ensure its financial viability. Consequently, \$221,531 of the Authority's public housing funds was not available for its intended purpose.

HUD granted a waiver for conflict-of-interest provisions and permitted the Authority to purchase insurance from a company that employed a board member. In its waiver, HUD cited good cause reasons and further noted that the insurance bid was the best and most reliable bid submitted. Therefore, we did not have an issue with the conflict of interest.

What We Recommend

We recommend that the Director of HUD's Office of Public Housing require the Authority to develop a plan to bring it into compliance with HUD's requirements and if necessary, ensure that the lender formally releases the HUD-related funds as collateral. As of December 31, 2008, the HUD-related certificate of deposit account put at risk totaled \$673,859. Also, we recommend that HUD require the Authority to propose a legal solution regarding the ownership structure of the nonprofit organization. If a legal solution is not possible, we recommend that HUD require the Authority to repay its public housing program \$221,531 in nonfederal funds or the current amount owed that the Authority advanced to its nonprofit organization.

In addition, HUD should require the Authority to (1) implement adequate controls and procedures to ensure that it does not encumber or spend HUD assets on nonfederal activities without HUD approval and (2) develop and implement a strategic, comprehensive marketing plan for the nonprofit organization to ensure that it becomes financially sound.

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 our review results with the Authority during the audit and with HUD officials during the exit conference. We provided a copy of the draft report to Authority officials on June 11, 2009, for their comments and discussed the report with the officials at the exit conference on June 25, 2009. The Authority provided written comments on July 2, 2009. The Authority disagreed with the findings but understands what must be done to fulfill HUD's mission. It agreed to seek to replace the letter of credit that encumbered the \$650,000, and implement controls and procedures designed to ensure it does not encumber or spend HUD assets on nonfederal activities without HUD approval.

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 OBJECTIVE

The Housing Authority of the City of Newnan (Authority), Georgia, was established in 1950 by the mayor and city council of Newnan. The mission of the Authority is to develop and operate each project solely for the purpose of providing decent, safe, and sanitary housing for eligible families in a manner that promotes serviceability, economy, and stability of the projects and the economic and social well-being of the tenants. The Authority's five-member board of commissioners oversees the direction of the Authority. The Authority administers 397 units of public housing and a Section 8 Housing Choice Voucher program that enables 68 families to rent from a private landlord with rental assistance that it administers.

The Authority created a domestic nonprofit organization, the Newnan Housing Development Corporation, on May 11, 2000, by resolution adopted by the governing body of the City of Newnan, Georgia, under the provisions of the Georgia Housing Authorities law for the purpose of carrying out the powers and any purposes of the Authority. The nonprofit entity is a controlled instrumentality of the Authority that developed 136 low-income apartment units located in Newnan, Georgia. The board members of the nonprofit organization are the members of the Authority's board.

The Authority received approximately \$18.3 million from the U.S. Department of Housing and Urban Development (HUD) to operate its various programs from January 1, 2000, through December 31, 2008. HUD's Georgia State Office of Public Housing in Atlanta, Georgia, is responsible for overseeing the Authority.

Our objective was to determine whether the Authority inappropriately used funds and assets restricted by its annual contributions contract with HUD to support the operations of its nonprofit organization and incurred costs for insurance that involved conflicts of interest.

RESULTS OF AUDIT

Finding 1: The Authority Inappropriately Encumbered Its Funds to Support Its Nonprofit Entity

The Authority inappropriately encumbered \$649,976 in HUD-restricted funds in violation of its annual contributions contract with HUD and also violated an agreement it made with HUD concerning the sale and disposition of Authority property. The Authority used the \$649,976 to open a certificate of deposit account as collateral to secure a bond issuance on behalf of its nonprofit organization. In addition, it encumbered its assets as collateral for a \$150,000 loan on behalf of the nonprofit organization. These encumbrances occurred because the Authority lacked the controls necessary to avoid encumbrances. As a result, the encumbrances put the Authority's funds at risk.

Criteria

Part A of the annual contributions contract, section 7, Covenant against Disposition and Encumbrances, states that the Authority shall not in any way encumber any such project, or portion thereof, without the prior approval of HUD. In addition, the Authority shall not pledge as collateral for a loan the assets of any project covered under the contract.

Public Housing Funds Encumbered

The Authority inappropriately encumbered \$649,976 in HUD-restricted funds in violation of its annual contributions contract with HUD and also violated an agreement it made with HUD concerning the sale and disposition of Authority property. Under its contract agreement with HUD, the Authority received the \$649,976 from the sale of real estate to the City of Newnan. HUD approved the disposition with the stipulation that the proceeds could only be used for housing which was owned and managed by the Authority.

The Authority allowed the nonprofit organization to use the \$649,976 to open a certificate of deposit account to secure an \$8.5 million bond issuance. The bond proceeds were used by the nonprofit entity to develop 136 low-income apartment units in Newnan, Georgia. The Authority manages the housing complex, but it does not own the housing, which was required by the HUD approval. As of December 31, 2008, the certificate of deposit account balance was \$673,859, which included interest earned.

The Authority's executive director initiated efforts during our audit to obtain a modification to HUD's disposition agreement that would permit the Authority to use the \$649,976 in sale proceeds on behalf of the nonprofit organization. On May 20, 2009, HUD's Special Applications Center provided a response to the Authority. However, HUD's Georgia State Office of Public Housing reviewed the response and determined that the modification to HUD's disposition agreement did not allow the Authority to use the sale proceeds for anything other than low income public housing as defined by the U.S. Housing Act of 1937 and therefore the sale proceeds could not be used for the nonprofit organization.

In addition, the Authority violated its annual contributions contract provision against encumbrances when it obtained a loan for \$150,000 to pay preliminary expenses associated with proposed acquisition, design, development, and financing for the nonprofit organization. The Authority encumbered its assets when it pledged them as collateral for the \$150,000 loan if the nonprofit entity could not make the loan payments. Although the loan was repaid, the nonprofit organization was not financially sound, and the encumbrance placed the Authority's funds at risk.

The Authority lacked the controls necessary to avoid encumbrances. Its board of commissioners did not have adequate controls in place to keep it from encumbering the Authority's federal assets when pursuing nonfederal housing ventures. Although the executive director was aware of HUD's provision against encumbering assets, when she signed the loan documents and agreements, she was unaware that the loan agreements included clauses that pledged the Authority's assets if the nonprofit organization did not pay off the loan.

Recommendations

We recommend that the Director of HUD's Office of Public Housing

- 1A. Require the Authority to develop a plan to bring the Authority into compliance with HUD's requirements and if necessary, ensure that the lender formally releases the HUD-related funds as collateral. As of December 31, 2008, the HUD-related certificate of deposit account put at risk totaled \$673,859.
- 1B. Require the Authority to implement adequate controls and procedures to ensure that it does not encumber HUD assets for nonfederal activities without HUD approval.

Finding 2: The Authority Inappropriately Advanced Funds to Support Its Nonprofit Entity

The Authority inappropriately used \$221,531 of its public housing program funds for nonfederal development activities in violation of its annual contributions contract with HUD. In addition, it inappropriately used HUD funds to make 31 monthly payments on a \$150,000 loan on behalf of its nonprofit organization. This condition occurred because the Authority's board of commissioners did not establish sufficient controls to ensure that the executive director followed terms and conditions established in the contract. Also, the nonprofit organization was not financially sound, and the Authority did not have an updated comprehensive marketing strategy to ensure its financial viability. Consequently, \$221,531 of the Authority's public housing funds was not available for its intended purpose.

Criteria

Part A of the annual contributions contract, section 9, Depository Agreement and General Fund, (C), states that the Authority may withdraw funds from the general fund only for the payment of the costs of development and operation of the projects under the annual contributions contract with HUD.

\$221,531 Advanced to Nonprofit Organization

The Authority inappropriately advanced \$221,531 to its nonprofit organization to pay expenses that it had incurred. The nonprofit organization's revenue was insufficient to pay its financial obligations, and the Authority paid the operational costs that the nonprofit entity could not pay. Consequently, the balance due to the Authority grew steadily from \$11,161 in July 2006 to \$221,531 in February 2009. The nonprofit organization did not have the funds needed to repay the accounts receivable balance it owed the Authority. Therefore, the Authority was at risk of losing \$221,531 in public housing funds intended to benefit its residents and programs supported by HUD.

In addition, the Authority inappropriately paid 31 monthly loan payments of approximately \$2,900 on behalf of the nonprofit organization. The Authority obtained a loan for \$150,000 to pay preliminary expenses associated with proposed acquisition, design, development, and financing for the nonprofit entity. The nonprofit organization then repaid the Authority the 31 payments and made

the remaining monthly loan payments until the loan was repaid. Although the nonprofit entity repaid the Authority the 31 payments, the Authority violated section 9 of its annual contributions contract with HUD when it used HUD funds to support the operations of its nonprofit organization.

Authority management did not have adequate controls in place to ensure that its restricted federal funds were only used for the payment of the costs of development and operation of the projects under the contract with HUD. The Authority's board of commissioners did not have a monitoring process to ensure that the Authority did not use its federal funds for nonfederal development efforts.

Updated Comprehensive Marketing Strategy Needed to Ensure Financial Viability

The Authority's nonprofit entity did not have a current written marketing plan. In October 2004, a written marketing plan was developed. The Authority and its related nonprofit organization had taken a variety of actions to market the property, and they had taken steps to monitor its progress. For example, the nonprofit entity's property manager maintained a weekly management report on the marketing status of the apartments. Other efforts to market the nonprofit organization included newspaper advertisements, offering a \$99 move-in special, payment arrangements for the security deposit, and a \$1,000 referral fee for tenants. The nonprofit organization's property manager attended a Section 8 voucher seminar to inform tenants that they could use their housing choice vouchers in Newnan, Georgia. Although various marketing efforts were tried, the nonprofit remained financially unsound.

The nonprofit organization would likely benefit from a current marketing plan that strategically and comprehensively addresses various marketing components that would include but not necessarily be limited to assessments of locality-based rents, census and demographic studies, locality-based vacancy rates, effective advertising, and incentives.

Recommendations

We recommend that the Director of HUD's Office of Public Housing

- 2A. Require the Authority to propose a legal solution regarding the ownership structure of the nonprofit organization. If a legal solution is not possible, the Director should require the Authority to repay its public housing program \$221,531 in nonfederal funds or the current amount owed that the Authority advanced to its nonprofit organization.
- 2B. Require the Authority to implement adequate controls and procedures to ensure that it does not spend HUD assets on nonfederal activities without HUD approval.
- 2C. Require the Authority to develop and implement a strategic, comprehensive marketing plan for the nonprofit organization to ensure that it becomes financially sound.

SCOPE AND METHODOLOGY

To accomplish our objective, we

- Considered Office of Inspector General (OIG) concerns that the Authority may have encumbered assets, used its restricted funds for nonprofit activities, and violated conflict-of-interest provisions;
- Researched HUD handbooks, the *Code of Federal Regulations*, the annual contributions contract, and other requirements and notices that govern the Authority's public housing programs;
- Reviewed the Authority's board minutes, financial statements, audit reports, records, bank statements, and security instruments pertaining to the development and operations of the nonprofit organization;
- Reviewed the Authority's marketing plans for the nonprofit organization and the Authority's cost allocation policy and procedures;
- Reviewed the nonprofit organization's incorporation documents and related correspondence;
- Interviewed officials of the HUD Georgia State Office of Public Housing and Regional Counsel attorney advisors, Authority management and staff, and nonprofit organization staff.

Our audit generally covered the period January 1, 2000, through December 31, 2008. We expanded our scope as necessary to complete our objective. We performed our audit from February through May 2009 at the Authority's office located in Newnan, Georgia, and at HUD's Georgia State Office of Public Housing located in Atlanta, Georgia.

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. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

INTERNAL CONTROLS

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

- Compliance with laws and regulations - Policies and procedures that management has implemented to reasonably ensure that its resources are used in accordance with laws and regulations.
- Safeguarding of 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 internal controls do not provide reasonable assurance that the processes 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 items are significant weaknesses:

- The Authority did not adequately monitor the use of its funds to ensure that its assets were not encumbered for activities not related to the development and operation of public housing under its annual contributions contract agreement with HUD (see finding 1).
- The Authority did not adequately monitor its disbursement of federal funds to ensure that payments were for supported and eligible housing activities (see finding 2).

APPENDIXES

Appendix A

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

| <u>Recommendation number</u> | <u>Ineligible 1/</u> | <u>Funds to be put to better use 2/</u> |
|----------------------------------|----------------------|---|
| 1A | | <u>\$673,859</u> |
| 2A | <u>\$221,531</u> | |
| Total | <u>\$221,531</u> | <u>\$673,859</u> |

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or federal, state, or local policies or regulations.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. For recommendation 1A, the \$673,859 represents encumbered funds that could be used by the Authority for activities supported by its annual contributions contract with HUD as intended.

Appendix B


AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Housing Authority of Newnan

"Meeting the Challenge for Affordable Housing"



President/CEO:
Sandra M. Strozier

Commissioners:

Willie Pritchett
Chairman

Otis Jones, III
Vice Chairman

Jack Binion

Carolyn Andrews

Eleanor Goode

July 2, 2009

To: James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA

From: Sandra Strozier, Executive Director Newnan Housing Authority

Subject: The Housing Authority of the City of Newnan, Georgia, Inappropriately Encumbered Assets and Advanced Funds to Support Its Nonprofit Organization

First we would like to thank the auditors for their professionalism throughout this process and for the insight provided on matters during the course of this examination. While we disagree with all of finding 1 and feel that parts of finding 2 should be revised, HAN staff understands we are all doing our part to fulfill HUD's mission.


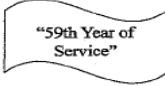
Response to finding 1

The empirical evidences which has been available to the Newnan Housing Authority (HAN) staff and which it has made available to the auditors would seem to suggest finding 1 ***The Authority Inappropriately Encumbered Its Funds to Support Its Nonprofit Entity***, should not be a finding reportable in the final report. It is our request that this finding be removed based upon the following discussion.

On numerous occasions and throughout the process HAN communicated with the HUD Special Applications Center (SAC) in Chicago, IL regarding its intent to dispose of Joseph E. Hannah Homes, GA095001 and Hannah Homes additions, GA095003 and construct low and mixed-income units. The HAN staff has written approval from SAC to dispose of 9.79 acres. Additionally, SAC granted approval to HAN to use the proceeds to construct 139 low and mixed-income units. In a letter to the HAN, SAC stated, the HAN will receive net proceeds from this disposition; the HAN is authorized to use the proceeds from the sale for the acquisition or

1

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Comment 1

construction of low-income housing as defined by the U.S. Housing Act of 1937.

The HAN mission is to develop and operate decent, safe and sanitary housing for eligible families which is one of the major tenors of the U.S. Housing Act of 1937. The Summit Point Apartments are decent, safe and sanitary housing. The rents are 8% - 10% lower than the FMR in the area. The community has between 20-25 Housing Choice Voucher participants as residents at any given point in time. This represents 15% - 18% of the Summit Point units. Over 40% of all residents living in Summit Point Apartments make less than 50% of the area median income. After disposition of Joseph E. Hannah Homes and Hannah Homes additions coupled with the fact that the City of Newnan did not plan to build any replacement units, Summit Point Apartments were needed to preserve the HAN's affordable housing stock.

As required by 24 CFR, Section 970.14 of the regulations, the HAN kept the Georgia State Office informed regarding the status of the process to construct the new housing.

The HUD Office provided a certification stating that the subject submission accurately describes the project proposed for disposition and the reasons provided by the HAN to support the proposed action are correct and factual.

After discussions with the HAN board of directors and others involved in the process it was determined that the best way to finance and construct this new housing was to issue Tax-Exempt Housing Bonds. It was also decided that a new not-for-profit corporation would be formed to account for this project. From the outset, HAN intended to have complete control of the new development as it would manage the project once the construction was complete. The board of directors which served the HAN would also serve the newly developed corporation. Summit Point Apartments were successfully completed, thereby, increasing the number of affordable units serving this community and improving the quality of the overall units available.

The disposition of the original housing stock by HAN and the net proceeds derived are considered to be a Section 18 Disposition. The guidelines regarding Section 18 Dispositions state:

If any proceeds remain after the PHA has paid for the costs of disposition, these proceeds are known as net proceeds. PHAs may use net proceeds for leveraging of amounts for securing housing developments that include public housing (ACC) units or units assisted by the Housing Choice Voucher Program (Section 8 units).

2

Comment 1

While Summit Point Apartments does not have any ACC units, as a mixed-income housing project the intent was always to have section 8 tenants. There is a large number of section 8 residents living in the project (20 – 25 families). Accordingly, HAN staff believes Summit Point Apartments satisfies this requirement under the Section 18 Dispositions guidelines. Let it also be noted that the Authority still plans to add additional ACC units by way of acquisition. We have already purchased 4 single-family homes and we plan to purchase additional units utilizing our Replacement Housing Funds.

The guidelines also state:

A PHA may use proceeds as “leverage” in order to partner with a private entity for the purpose of developing mixed-finance housing.

By securing the CD which is the subject of finding 1 and using it as leverage HAN did exactly what is expressly stated within the guidelines.

Finding 1 states: “HUD approved the disposition with the stipulation that the proceeds could only be used for housing which was owned and managed by the Authority”. While the audit does state that the project is managed by HAN which is correct, HAN would carry this discuss out further. Not only is the project managed by HAN, Summit Point is included as a component unit and reported on HAN’s FDS. The HAN and Summit Point have a common board of directors and section 18 dispositions funds can be used to form partnerships with private entities for the purpose of developing mixed-finance housing. *The Newnan Housing Development Corporation is a non-profit entity own by the Housing Authority of Newnan.*

On June 9, 2003, the HAN submitted its Section 18 Disposition Application to HUD. The letter clearly states, “The Proceeds from the sale of the above mentioned property will be pledged to preserve thirteen elderly units as either public housing or project based assisted units”, the letter goes on to say that “This new construction is a Tax-Exempt Bond Financed, multi-family, mixed income project being developed by our non-profit entity Newnan Housing Development Corporation”. The Special Application Center of HUD was informed from the beginning of the project that the Non-Profit entity of the Authority (Newnan Development Corporation) would own the apartments. The creation of the Newnan Housing Development Corporation was done for two primary reasons. First, it gives the HAN a defined way in which to account for the project. Second, it insulates the HAN and HUD from the \$8 million debt required to build the project.

In a letter to SAC from the HAN dated July 21, 2004 it was stated: "The Housing Authority will use the proceeds of the sale as collateral for the financing of our newly built affordable housing apartment".

Nowhere throughout this project was there an attempt by the HAN to shield anything it was doing as a part of this project. Approvals were solicited and secured at each step of the project. Based on the volume of documentation on file with the HAN every attempt was made to remain as transparent as possible. Accordingly, HAN is proud of the integrity which was maintained through this project and equally as proud of the new affordable housing provided to the residents of Newnan, GA.

Comment 1

On May 20, 2009, the HAN obtained an amendment to the original Disposition Application approved on April 28, 2004. This letter provides further clarification to the use of the proceeds. The HAN was given permission to use the proceeds "for the acquisition or construction of low-income housing as defined by the U. S. Housing Act of 1937", in that request we informed the SAC again that the Newnan Housing Development Corporation was the owner of the property. Because of the fact that finding 1 is mis-leading on a number of different fronts and the fact that there were no funds which were inappropriately encumbered, we respectfully request that finding 1 not be reported in the final report.

The HAN proposes to comply with the recommendations in the following manner:

Comment 2

1. We request that the ownership of the Newnan Housing Development Corporation (NHDC) remain as is. The NHDC is a Component Unit of the HAN consequently; HAN controls the asset own by the NHDC (Summit Point).

Comment 3

2. The HAN will seek to replace the Letter of Credit that encumbered the \$650,000 CD and at that occurrence the \$650,000+ will be transferred back to the HAN. However, it is important to note that this decision is a bank decision but we will do everything within our power to promote this decision.

Comment 3

3. The HAN will implement controls and procedures designed to help ensure it does not encumber or spend HUD assets on nonfederal activities without HUD approval. We will do this by adopting the following procedures:

- All contracts, agreements and legal documents containing financial liability or encumbrances will be reviewed by local legal counsel and Board of Commissioner before signing and the following statement will be added.

"Notwithstanding anything contained herein to the contrary, repayment shall not be payable from any revenues or other funds designated for certain purposes restricted by the payor of such funds, including, but not limited to any restricted purpose funds or revenues received, directly or indirectly from U.S. Department of Housing and Urban Development and any revenues or other funds of HAN that are otherwise encumbered, restricted or designated by HAN for any other purpose."

Response to finding 2

Comment 4

As a result of the economy and the housing shadow market the nonprofit organization under which the asset of Summit Point is accounted for is not financially sound and HAN fully agrees with this assertion. However, the implied thoughts that the nonprofit and HAN are not working diligently to improve the financial viability of the nonprofit is an assertion which the HAN's staff disagrees.

As mentioned earlier, the shadow market which is where apartment owners are now competing with single family dwellings at comparable rents has many former apartment dwellers moving to single family units. Since Summit Point is the only asset of the nonprofit this shadow market is especially devastating since there are no other assets from which it can draw the needed revenue.

HAN has kept records of all of the transactions between it and the nonprofit and has appropriately accounted for these transactions on its books and in its records. In order to alleviate some of the financial pressure of the nonprofit, the HAN has developed a comprehensive plan to refinance the debt which is currently being carried by the nonprofit and it is in discussion which the holder's of that debt and the bank is listening and cooperating in an effort to get the debt service down to a more manageable level.

Comment 5

Of the \$329,531 reported in finding 2, approximately \$140,000 is management fees which are due to the Central Office. Since Central Office funds are de-federalized, we are requesting that the \$140,000 be deducted from the \$329,531. Again, this is in an effort to reduce the debt of the project and safeguard the asset and all of its collateral.

As for the marketing of Summit Point, the management is doing what it can to stop of the loss of tenants who are moving out because they can get a single family dwelling for a comparable monthly rent. This issue is systemic within the Newnan community and given our best marketing efforts this continues to be an issue when owners of property who would otherwise sale their properties are now renting those units.

The HAN proposes to comply with the recommendations in the following manner:

Comment 6

1. We request that the ownership of the Newnan Housing Development Corporation (NHDC) remain as is. The NHDC is Component Unit of the HAN consequently; HAN controls the asset own by the NHDC. (Summit Point)

Comment 6

2. The HAN propose that the \$329,531 minus \$140,000 be disposed of as follows:

- a. The NHDC as a component unit of the HAN and shares a common Board we will make the proposal to the Board that this debt be forgiven or
- b. The debt will become a long-term repayment agreement.

Comment 7

3. The HAN will implement adequate controls and procedures to ensure that it does not encumber or spend HUD assets on nonfederal activities without HUD approval. We will do this by adopting the following procedures:

- All contracts, agreements and legal documents containing financial liability or encumbrances will be reviewed by local legal counsel and Board of Commissioner before signing and the following statement will be added.

"Notwithstanding anything contained herein to the contrary, repayment shall not be payable from any revenues or other funds designated for certain purposes restricted by the payor of such funds, including, but not limited to any restricted purpose funds or revenues received, directly or indirectly from U.S. Department of Housing and Urban Development and any revenues or other funds of HAN that are otherwise encumbered, restricted or designated by HAN for any other purpose."

Comment 8

4. The HAN will expand upon current marketing strategies to help ensure that the property become financially sound.

Cc: Ada Holloway, Director, Office of Public Housing, 4APH

OIG Evaluation of Auditee Comments

Comment 1 The Authority disagreed with the finding. The Authority's comments cited numerous communications with HUD when requesting approval to dispose of the property. The Authority stated it had written approval from HUD's Special Applications Center to dispose of the land, as well as approval to construct 139 low and mixed-income units.

The memorandum of approval from the Special Applications Center restricted the use of the sales proceeds for housing that was owned and managed by the Authority. The Authority managed the nonprofit and the same members served on both the Authority board and the nonprofit board. However, the Authority did not own the nonprofit apartments. The nonprofit apartment units were not under HUD's control within the annual contributions contract agreement and the recorded deed showed that the nonprofit entity owned the property. HUD's Georgia State Office of Public Housing reviewed the May 20, 2009, Special Applications Center amendment and determined that the modification to HUD's disposition agreement did not allow the Authority to use the sale proceeds for anything other than low income public housing as defined by the U.S. Housing Act of 1937, and therefore the sale proceeds could not be used for the nonprofit organization and the encumbrance was inappropriate.

Comment 2 The Authority requested that the ownership structure of the nonprofit remain as is. However, HUD and the Authority need to develop a mutually agreeable solution that will bring the Authority into compliance with HUD's requirements and if necessary ensure that the lender formally releases the HUD-related funds as collateral.

Comment 3 The Authority's agreement with the recommendations to seek to replace the letter of credit that encumbered the \$650,000, and implement controls and procedures indicates its willingness to make the necessary corrections.

Comment 4 We acknowledge that the Authority has tried a variety of marketing strategies and had a marketing plan in 2004; however, the nonprofit has remained financially unsound despite those efforts.

Comment 5 The Authority stated that \$140,000 of the \$329,531 represents management fees that are due its central office; therefore, it requested that the \$140,000 be deducted from the \$329,531.

The Authority converted to asset management accounting on July 1, 2007. The management fees earned from July 2006 through February 2009 were \$128,000, which included \$20,000 earned before the conversion, and are funds due under the annual contribution contract agreement. Therefore, \$108,000 should be

deducted from the \$329,531. We revised our recommendation to show that the Authority should repay HUD \$221,531 versus \$329,531. The additional \$12,000 (\$140,000 - \$128,000) was earned after we completed our review and are not included in the \$329,531.

Comment 6 The Authority requested that the ownership structure of the nonprofit remain as is. However, HUD and the Authority need to develop a mutually agreeable solution that will repay the public housing program \$221,531 in nonfederal funds or the current amount owed that the Authority advanced to its nonprofit organization.

Comment 7 The Authority's agreement with the recommendation to implement controls and procedures indicates its willingness to make the necessary corrections.

Comment 8 The Authority's agreement with the recommendation to develop and implement an updated marketing strategy indicates its willingness to make the necessary corrections.