



Issue Date September 29, 2009

Audit Report Number 2009-AT-1014

TO: Michael A. Williams, Director, Office of Public Housing, Greensboro, NC,
4FPH

//signed//

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

SUBJECT: The Housing Authority of the City of Winston-Salem, North Carolina, Needs to
Improve Financial Controls

HIGHLIGHTS

What We Audited and Why

We reviewed the Housing Authority of the City of Winston-Salem (Authority) because it will receive \$3.9 million for capital fund projects under the American Recovery and Reinvestment Act of 2009 (ARRA). In addition, the Secretary of the U. S. Department of Housing and Urban Development (HUD) received a citizen's complaint alleging that the Authority used unethical procurement practices.

Our objectives were to (1) evaluate the Authority's capacity in the areas of internal controls, eligibility, financial controls, procurement, and output/outcomes in administering funds and (2) determine whether the Authority followed federal procurement regulations.

What We Found

The Authority was generally prepared to properly administer the ARRA capital funds, but it did not have adequate financial controls to achieve the ARRA objective of transparency and accountability. ARRA contains five crucial

objectives to ensure transparency and accountability, one of which is that funds are spent for authorized purposes and not wasted. The Authority had successfully completed projects with 2005, 2006, and 2007 capital fund grants and complied with requirements in preparation for receiving the ARRA capital funds. However, the Authority's policies and procedures were not sufficient to ensure that previous capital funds were properly spent. This condition resulted in more than \$2 million in unsupported and \$81,869 in ineligible capital fund expense reimbursements.

The Authority generally followed federal procurement regulations. We reviewed 4 capital fund construction contracts for the 2005, 2006 and 2007 grants, 4 contracts from the 62 shown on the contract log, and 4 purchase order procurements not included on the contract log. We did not find deviations from the federal procurement regulations.

What We Recommend

We recommend that HUD increase oversight of the Authority's administration of ARRA funds and require it to implement appropriate financial policies, procedures, and controls. In addition, the Authority must provide support for more than \$2 million in unsupported capital fund reimbursements or repay the funds and repay \$81,869 in ineligible capital fund expense reimbursements.

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 provided the draft report to the Authority on September 24, 2009, and discussed the findings with Authority officials at an exit conference on September 24, 2009. The Authority provided its written comments on September 24, 2009. It agreed with the \$2 million in unsupported costs but expressed disagreement with the need for increased HUD oversight as well as some of the ineligible costs.

The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

TABLE OF CONTENTS

Background and Objectives	4
Results of Audit	
Finding 1: The Authority Did Not Have Adequate Financial Controls	5
Scope and Methodology	8
Internal Controls	9
Appendixes	
A. Schedule of Questioned Costs	10
B. Auditee Comments and OIG's Evaluation	11

BACKGROUND AND OBJECTIVES

The Housing Authority of the City of Winston-Salem (Authority) was formed in 1941 pursuant to the North Carolina Housing Authorities Law. Its primary objective is to provide low-income housing to the citizens within Winston-Salem, North Carolina, and the surrounding area in compliance with its annual contributions contract with the U.S. Department of Housing and Urban Development (HUD). It is governed by a nine-member board of commissioners appointed by the mayor of Winston-Salem. The Authority's records are located at 500 West Fourth Street, Suite 300, Winston-Salem, North Carolina.

In addition to its regular 2008 capital fund allocation of \$1.8 million, HUD allocated the Authority an additional \$3.9 million in formula-based capital funds under the American Recovery and Reinvestment Act of 2009 (ARRA). Enacted as Public Law 111-5 on February 17, 2009, Division A, Title XII of ARRA provides \$3 billion in formula-based and \$1 billion in competitive capital funds to public housing authorities to carry out capital and management activities, as authorized under Section 9 of the United States Housing Act of 1937. On March 3, 2009, HUD amended the annual contributions contract with the Authority to include the formula-based capital funds to ensure that public housing developments continue to be available to serve low-income families. HUD approved the Authority's planned use of the funds to include appliances (\$241,000), air conditioning/heating units (\$441,000), and upgrades (\$2,570,000) at Cleveland Avenue Homes, Sunrise Towers, Crystal Towers, and the Townview Apartments, along with more than \$609,000 for planning and administration costs. As of August 13, 2009, the Authority had obligated about 60 percent of the ARRA funds but had not spent any of the funds. The Authority plans to apply for additional competition-based capital funds available under ARRA.

Our objectives were to (1) evaluate the Authority's capacity in the areas of internal controls, eligibility, financial controls, procurement, and output/outcomes in administering funds and (2) determine whether the Authority followed federal procurement regulations.

RESULTS OF AUDIT

Finding 1: The Authority Did Not Have Adequate Financial Controls

The Authority was generally prepared to properly administer the ARRA capital funds, but it did not have adequate financial controls to achieve the ARRA objective of transparency and accountability. ARRA contains five crucial objectives to ensure transparency and accountability, one of which is that funds are spent for authorized purposes and not wasted. The Authority had successfully completed projects with 2005, 2006, and 2007 capital fund grants and complied with requirements in preparation for receiving the ARRA capital funds. However, its policies and procedures were not sufficient to ensure that previous capital funds were properly spent. This condition resulted in more than \$2 million in unsupported and \$81,869 in ineligible capital fund expense reimbursements.

The Authority Had Unsupported/Ineligible Capital Fund Expense Reimbursements

The Authority's capital fund program was operated on a reimbursement basis. It would incur expenses and then submit reimbursement requests through HUD's Line of Credit Control System. We reviewed more than \$4.7 million of the Authority's more than \$5.7 million in capital fund expense reimbursements for the 2005, 2006, and 2007 capital fund grants to determine whether the expenses were supported by source documents. For the reimbursed expenses supported by source documents, we reviewed the documents to determine whether the expenses were eligible for the capital fund program. The Authority could not provide supporting documentation for more than \$2 million in reimbursed capital fund expenses.

HUD regulations (24 CFR (*Code of Federal Regulations*) 85.20(b)(2)(6)) required the Authority to maintain accounting records that adequately identified the application of funds and were supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract documents, etc. We found reimbursement requests having few or no supporting documents and others that were well supported by contracts, invoices, and checks. Because the Authority did not maintain consistent supporting documentation, it could not show whether the \$2 million represented eligible capital fund expenses.

Grant year	Grant number	Authorized	Reimbursed	Tested	Supported	Unsupported
2005	NC19P012501-05	\$2,499,802	\$2,499,802	\$2,499,802	\$1,532,828	\$966,974
2006	NC19P012501-06	2,363,348	2,363,348	1,555,812	641,726	914,086
2007	NC19P012501-07	<u>2,633,868</u>	<u>852,740</u>	<u>703,105</u>	<u>539,851</u>	<u>163,254</u>
Totals		<u>\$7,497,018</u>	<u>\$5,715,890</u>	<u>\$4,758,719</u>	<u>\$2,714,405</u>	<u>\$2,044,314</u>

For more than \$2.7 million in reimbursements supported by source documents, the Authority was reimbursed \$81,869 for ineligible capital fund expenses. Federal cost principles in OMB Circular A-87 require that expenses be necessary and reasonable for efficient grant administration, and HUD Handbook 7485.3 contains specific capital fund expense limits and eligibility restrictions. The Authority was twice reimbursed for the same payroll expenses. It was reimbursed \$43,090 for payroll expenses under the 2006 grant and again for the same expenses after transferring the \$43,090 to the 2007 grant. Further, the Authority was reimbursed \$38,779 for operating expenses, such as car washes and plumbing repairs, charged to grant administration and site improvement that were not eligible capital fund expenses.

These deficiencies occurred because the Authority did not have adequate controls over the capital fund expense reimbursement process. The Authority had a grants administration policy, but it did not provide guidance regarding what was needed to support capital fund reimbursement requests. The grant accountant was not aware of this policy. She said that each director of finance processed reimbursements differently and she was not always sure what the reimbursements were for because there was nothing attached. We noted that the Authority had improved its reimbursement procedures by having the grant accountant maintain the invoices. However, it needs to make additional improvements because March 2009 reimbursement requests did not have a clear audit trail tying the invoices to the specific reimbursed expenses they were meant to support. Without improved controls, the Authority cannot provide the transparency and accountability required for the ARRA capital funds.

Recommendations

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

- 1A. Increase oversight of the Authority's administration of the ARRA capital funds in the area of financial controls.

- 1B. Require the Authority to implement financial policies, procedures, and controls to ensure that its reimbursements of ARRA capital fund expenses are adequately supported by source documents and are for eligible expenses.
- 1C. Require the Authority to provide the supporting source documents to show that the \$2,044,314 was for eligible capital fund expenses. If the Authority cannot provide adequate support, it should be required to reimburse the U.S. Treasury \$1,881,060 from nonfederal funds for the closed 2005 and 2006 capital fund grants and either provide \$163,254 in eligible capital fund expenses for the open 2007 grant or reimburse its 2007 capital fund grant using nonfederal funds.
- 1D. Require the Authority to reimburse the U.S. Treasury \$38,779 from nonfederal funds for ineligible capital fund expenses pertaining to the closed 2006 capital fund grant and either provide another \$43,090 in eligible capital fund expenses for the open 2007 grant or reimburse that grant using nonfederal funds.

SCOPE AND METHODOLOGY

Our objectives were to (1) evaluate the Authority's capacity in the areas of internal controls, eligibility, financial controls, procurement, and output/outcomes in administering funds and (2) determine whether the Authority followed federal procurement regulations.

To accomplish our objectives, we reviewed

- ARRA; federal financial management and procurement regulations at 24 CFR 85.20 and 85.36; federal cost principles in OMB Circular A-87; HUD Handbook 7485.3, Comprehensive Grant Guidebook, on capital fund grants; the supplement to HUD Handbook 7475.1, REV-1, CHG-1, Financial Management Handbook; HUD guidance on use of capital funds authorized by ARRA; Office of Inspector General (OIG) audit reports numbers 2005-AT-1802, 2006-AT-1005, and 2006-AT-1007; HUD's amended annual contributions contract with the Authority; and HUD's Greensboro Office of Public Housing's correspondence and files pertaining to the Authority.
- The Authority's policies and procedures manuals; planned use of the capital funds authorized by ARRA; previous capital fund budgets and reimbursements from HUD's Line of Credit Control System; contracts awarded for 2005, 2006, and 2007 capital fund grants; service and supply contracts; check registers; credit card statements; staffing assignments; job descriptions; and organization charts.

We also interviewed the Authority's employees and HUD's Greensboro staff involved with oversight of the Authority.

We performed our on-site audit work from May through July 2009 at the Authority's office located at 500 West Fourth Street, Suite 300, Winston-Salem, North Carolina. The audit covered the period January 2007 through April 2009 and was expanded as determined necessary.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

INTERNAL CONTROLS

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:

- Controls over the safeguarding of resources against waste, loss, and misuse.
- Controls over compliance with laws and regulations.

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's internal controls over financial management were inadequate (see finding 1).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

<u>Recommendation number</u>	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>
1C		\$2,044,314
1D	\$81,869	
Total	<u>\$81,869</u>	<u>\$2,044,314</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/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Authority Comments



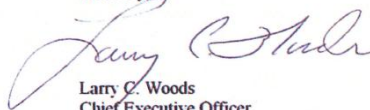
September 24, 2009

Mr. James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA
U.S. Department of Housing and Urban Development
Office of Audit, Box 42
Richard B. Russell Federal Building
75 Spring Street, SW, Room 330
Atlanta, GA 30303-3388

Dear Sir:

This letter is in response to your request for our comments on the draft report. I am attaching to this letter with our comments based on the format suggested. Please find attached "Auditee Comments". Please contact, if there are any questions at (336) 727-8500, ext. 105.

Sincerely,


Larry C. Woods
Chief Executive Officer
Housing Authority of Winston-Salem

Cc: Michael A. Williams
David Butcher

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Ref to OIG Evaluation

Authority Comments

Comment 1

Comment 1

Comment 1

Comment 2

<u>AUDITEE COMMENTS</u>	
<u>Ref to OIG Evaluation</u>	<u>Authority Comments</u>
1A	The Authority does not agree that there is a need for increased oversight. The Authority is currently has controls in place to assure accurate accounting and the proper expenditures of all funds. The information described in this report has been reviewed and audited in prior periods and found to be in compliance. These audits were done by outside auditors, Greensboro HUD office staff as well as the OIG offices. We are going back to track all expenditures for the grants reviewed. That information will be made available to the OIG staff and the Greensboro staff.
1B	Prior to the audit the Authority had put into place changes in the required documentation, financial policies, and procedures for reimbursements for the Capital program. All reimbursements are now carefully reviewed and proper documentation is available.
1C	The Authority agrees with this recommendation and is currently reviewing all the grants reviewed. We are retrieving all the prior period source documentation to assure HUD that all expenditures were proper and eligible. Although the Authority has provided this information in the past in prior, we will provide the source information for review and keep this information readily available for future reference.
1D	The Authority does not agree that the \$38,779 reimbursed by the treasury is ineligible and we are currently pulling the documentation for all capital fund reimbursements for 2005, 2006 and 2007. We request the opportunity to address this item with the total review for capital expenditures. We do agree with that an additional \$43,090 in expenditures should be supplied for the duplicate draw.
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OIG Evaluation of HUD Comments

- Comment 1** We found and included in the report that the Authority had made some improvement to its reimbursement procedures. However, some of the latest reimbursements we tested (March 2009) were not adequately supported. We did not find that other auditors, HUD staff, or OIG tested or found the reimbursements to be in compliance with the requirement that they be supported by the source documentation. Since 2006, OIG has issued 2 reports and 1 memorandum on the Authority, but none of these included a review of capital fund reimbursements. HUD staff said that they reviewed and approved contract actions and the payment of expenses as a result of the OIG audits but did not review capital fund reimbursements to determine whether the requested amounts were supported by source documents. The Greensboro HUD general engineer stated that he reviewed construction progress payments and approved those to be reimbursed with capital funds. During the audit we tested some reimbursements of construction progress payments and found these to be supported.
- Comment 2** Descriptions of the supporting documents did not show that they were eligible capital fund expenses. If the Authority locates documentation that it believes clearly shows that these were eligible, it should provide the documents to HUD for consideration.