



Issue Date November 8, 2010
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Audit Report Number 2011-PH-1003
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TO: Clifford Taffet, Director, Office of Affordable Housing Programs, DGH

//signed//

FROM: John P. Buck, Regional Inspector General for Audit, Philadelphia Region,  
3AGA

SUBJECT: The Pennsylvania Housing Finance Agency, Harrisburg, PA, Generally  
Administered Its Tax Credit Assistance Program Funded Under the Recovery  
Act in Accordance With Applicable Requirements

## **HIGHLIGHTS**

### **What We Audited and Why**

We audited the Pennsylvania Housing Finance Agency (Agency) because it received \$95.1 million in Tax Credit Assistance Program (Program) funds under the American Recovery and Reinvestment Act of 2009 (Recovery Act), which was the largest amount of these funds awarded in Region III.<sup>1</sup> Our objective was to determine whether the Agency administered its Program in accordance with the requirements of the Recovery Act and applicable U.S. Department of Housing and Urban Development (HUD) requirements.

### **What We Found**

The Agency generally administered its Program in accordance with Recovery Act and HUD requirements. However, it incurred ineligible costs totaling \$135,590 and could not support costs totaling \$151,936. In addition, it did not obtain required lobbying certifications from contractors and subcontractors, and it understated its job creation information that it reported to the Federal reporting Web site.

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<sup>1</sup> Region III encompasses Pennsylvania, Virginia, Maryland, West Virginia, Delaware and the District of Columbia.

## What We Recommend

We recommend that HUD require the Agency to reimburse its Program \$135,590 for the ineligible costs identified by the audit and provide documentation to support \$151,936 in unsupported costs identified by the audit or reimburse its Program from non-Federal funds for any costs that it cannot support. In addition, the Agency should obtain the required lobbying certifications from contractors and subcontractors and develop and implement controls to ensure that accurate job information is reported on the Federal reporting Web site.

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 a discussion draft audit report to the Agency on October 7, 2010, and discussed it with the Agency at an exit conference on October 13, 2010. The Agency provided written comments to the draft audit report on October 22, 2010. It agreed with the conclusions and recommendations in the report. The complete text of the Agency's response can be found in appendix B of this report.

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## **BACKGROUND AND OBJECTIVE**

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The Pennsylvania Housing Finance Agency (Agency) was established in 1972 by an act of the Pennsylvania General Assembly. The Agency's purpose is the financing of decent, safe, and affordable homes and apartments for the citizens of Pennsylvania. It is an independent public corporation that acts on behalf of the State government. The Agency depends on its own ability to generate revenues to carry out its activities and pay its obligations. It sells taxable and tax-exempt securities to finance houses and rental units for Pennsylvania. In addition, it administers housing programs on behalf of the State government. The Agency is also responsible for administering the Federal Low-Income Housing Tax Credit (LIHTC) program and is a subrecipient of the U.S. Department of Housing and Urban Development's (HUD) HOME Investment Partnerships Program (HOME). HOME funds are used to develop multifamily rental housing in all parts of the State that do not receive their own HOME entitlement funds.

A 14-member board governs the Agency. The board membership consists of the State treasurer, three cabinet secretaries of the State government, six private members appointed by the governor and confirmed by the Senate, and four members appointed by the leadership of the State Senate and the House of Representatives. The board appoints the Agency's executive director, who is also its chief executive officer.

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (Recovery Act) into law. The purpose of the Recovery Act is to jumpstart the Nation's ailing economy, with a primary focus on creating and saving jobs in the near term and investing in infrastructure that will provide long-term economic benefits. The Recovery Act appropriated \$2.25 billion under the HOME program heading for a Tax Credit Assistance Program (Program) grant to provide funds for capital investments in LIHTC projects. HUD awarded Program grants to the 52 State housing credit agencies. On June 26, 2009, HUD awarded the Agency \$95.1 million in Program funds.

Although Program funds were appropriated under the HOME heading, these funds are not subject to any HOME requirements other than the environmental review and can only be used in LIHTC projects, which are administered through the U.S. Department of the Treasury. Program assistance may only be provided to a qualified low-income project for which a State housing credit agency has made an allocation of LIHTC under Section 42 of the Internal Revenue Code. Program assistance can only be provided to projects that were awarded LIHTCs during the period October 1, 2006, to September 30, 2009. The State housing credit agency is responsible for the use of its Program grant. Program funds must be used for capital investment in eligible LIHTC projects. Capital investment means costs that are included in the "eligible basis" of a project under Section 42 of the Internal Revenue Code. The "eligible basis" includes site acquisition costs; constructions costs; and architect, developer and legal fees. Program funds cannot be used for the administrative costs of the State housing credit agency including the cost of operating the program or monitoring compliance. The State housing credit agency is required to distribute Program funds competitively and pursuant to its qualified allocation plan. The State housing credit agency is also required to give priority to eligible projects that are expected to be

completed within 3 years from the date of the Recovery Act enactment or by February 16, 2012. Since a major purpose of Program funds is to immediately create new jobs or save jobs at risk of being lost due to the current economic crisis, the Recovery Act establishes deadlines for the commitment and expenditure of grant funds and requires State housing credit agencies to give priority to projects that will be completed by February 16, 2012.

As of July 4, 2010, the Agency had committed \$81.7 million and disbursed \$36.1 million of the \$95.1 million in Program funds to 28 LIHTC projects. The 28 projects consist of 16 elderly and 12 family projects, which will create or rehabilitate 1,271 assisted housing units. The Agency was in the process of committing the remaining Program funds to three LIHTC projects.

Our objective was to determine whether the Agency administered its Program in accordance with the requirements of the Recovery Act and applicable HUD requirements.

## RESULTS OF AUDIT

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### Finding: The Agency Generally Administered Its Program in Accordance With Applicable Requirements

Overall, the Agency administered its Program in accordance with the Recovery Act and HUD requirements. Specifically, it (1) met the required fund commitment deadline, (2) completed environmental clearances and obtained HUD approval of requests for release of funds before executing written agreements, (3) executed written agreements that complied with requirements, (4) received and disbursed Program funds in a timely manner, and (5) met increased transparency and reporting requirements. However, although the audit disclosed no material deficiencies with the Agency's Program, the Agency incurred ineligible costs totaling \$135,590 and could not support costs totaling \$151,936. In addition, it did not obtain lobbying certifications from contractors and subcontractors as required, and it understated its job creation information that it reported to the Federal reporting Web site.

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#### **The Agency Met the Required Commitment Deadline**

Under the Recovery Act and HUD's Office of Community Planning and Development (CPD) Notice CPD-09-03-REV,<sup>2</sup> the Agency was required to commit at least 75 percent of its Program grant of \$95.1 million by February 16, 2010. The Agency committed \$79.7 million, or 84 percent, of its Program funds by February 16, 2010. The Agency committed these funds to 26 projects. As of July 4, 2010, the Agency had committed \$81.7 million to 28 projects, and it was in the process of committing the remaining Program funds to 3 additional projects. Additionally, the Recovery Act limited Program funds to be used only for qualified low-income projects to which the State housing credit agency awarded LIHTCs during the period October 1, 2006, to September 30, 2009. The Agency complied with this requirement.

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<sup>2</sup> Revised July 27, 2009

**Environmental Clearances  
Were Completed and Requests  
for Release of Funds Were  
Approved Before Written  
Agreements Were Executed as  
Required**

Under HUD Notice CPD-09-03-REV, the Agency was required to complete an environmental clearance and obtain a HUD-approved request for release of funds before executing written agreements with project owners. The Agency complied with these requirements.

**The Agency's Written  
Agreements Complied With  
Requirements**

HUD Notice CPD-09-03-REV required the Agency to execute legally binding written agreements with each project owner. The written agreements were required to set forth all of the Program and crosscutting Federal grant requirements applicable to the funding and make these requirements enforceable through the recordation of a restriction that is binding on all owners. The Agency's written agreements generally complied with these requirements. The Agency supplemented the written agreements by requiring projects to execute an indenture of restrictive covenants for LIHTC and the Program, a mortgage note, and a Program guaranty.

**The Agency Received and  
Disbursed Program Funds in a  
Timely Manner**

The Agency drew down Program funds from HUD's automated Line of Credit Control System only when the payments were due. Our review of disbursements totaling \$9.7 million showed that the Agency disbursed the funds within 3 working days as required by HUD Notice CPD-09-03-REV.

**The Agency Met Increased  
Transparency and Reporting  
Requirements**

Under the Recovery Act and HUD Notice CPD-09-03-REV, the Agency was required to post on its Web site a description of its competitive selection criteria

for awarding Program funds to eligible projects. The Agency was also required to identify all projects selected for funding and post the amount of each Program award on its Web site. The Agency complied with these requirements.

### **Not All Program Expenditures Were Eligible or Adequately Supported**

The Agency did not ensure that all expenditures of Program funds were eligible and adequately supported. Our review of five project files indicated that the Agency incurred \$135,590 in ineligible costs and \$151,936 in unsupported costs. The ineligible costs of \$135,590 included \$124,124 in Program funds for the funding of escrow accounts. HUD Notice CPD-09-03-REV prohibits the funding of escrow accounts. The Agency also used \$11,466 in Program funds to pay construction-related costs for commercial space at a residential project. The Agency did not include the construction costs for the commercial space as eligible costs under Section 42 of the Internal Revenue Code. Since these costs were not included in the eligible basis of the project, the costs are ineligible. Further, the Agency's cost certification guide states that for developments that contain commercial space that the tenants will be charged to use, the cost of this space is not includable in the eligible basis. Agency staff members informed us that they were not aware of the Program requirements regarding the escrow accounts. Regarding the commercial space, Agency staff members stated that they did not notice that the construction costs included commercial space.

The unsupported costs of \$151,936 included \$141,936 for legal services for one project and \$10,000 for accounting services for another project. The Agency's documentation was not sufficient to determine whether these costs were eligible under the Program. Although the Agency had copies of invoices to support the legal services, the invoices lacked sufficient detail to determine whether the costs for meetings and reviewing correspondence and documentation related to the project. The purposes of the meetings and the subjects of the correspondence and documentation reviewed were unknown. Similarly, regarding the accounting services, the invoice did not indicate what specific service was provided and how the services related to the project. Office of Management and Budget (OMB) Circular A-87<sup>3</sup> states that for a cost to be allowable, it must be necessary and reasonable and adequately documented. Further, regarding legal fees, the Agency's development cost limits require fees to be itemized, specifically detailing work for property real estate, acquisition legal expenses, obtaining financing, and syndication costs. Agency staff members agreed that additional documentation should have been provided to support these services.

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<sup>3</sup> This policy guidance was relocated to 2 CFR, Subtitle A, Chapter II, Part 225.



### **The Agency Did Not Obtain Lobbying Certifications as Required**

Regulations at 24 CFR (Code of Federal Regulations) Part 87 prohibit Program funds from being used for lobbying activities. To comply with this requirement, all Program contractors and subcontractors that receive more than \$100,000 in funds must submit a certification for contracts, grants, and cooperative agreements. The Agency did not possess documentation to demonstrate that it met this requirement. Without the certifications, the Agency has no assurance that contractors and subcontractors refrained from lobbying. Agency staff members informed us that they were not aware of this requirement and were taking action to address the issue.

### **The Agency Understated Its Job Creation Information That It Reported to the Federal Reporting Web Site**

Although the Agency reported job information by the required deadlines, it did not ensure that the information it reported was complete and accurate. OMB Recovery Act implementation guidance states that data quality is an important responsibility of key stakeholders identified in the Recovery Act. The Agency, as the owner of the data submitted, has the principal responsibility for the quality of the information submitted. Our test of a sample of contractors and subcontractors that submitted payroll time sheets for the quarter ending June 30, 2010, showed that job calculator forms which the Agency used to report job information did not agree with the supporting time sheets. We compared the time reported on the payroll time sheets to the time reported on the job calculator forms and determined that two subcontractors underreported the number of hours worked during the quarter by 627 hours. Agency staff members stated that the primary reason the number of hours reported was understated was because of timing. The Agency requires contractors and subcontractors to submit payroll time sheets within a week after the end of the pay period. Because the general contractors have to submit their job calculator form to the project owner and then to the Agency by a certain time, the payroll information for the last two pay periods in the quarter (pay periods ending June 20 and June 27, 2010) were not included in the totals shown on the job calculator forms. In an effort to meet the Recovery Act goal of achieving unprecedented levels of accountability and transparency in government spending, the Agency should develop and implement controls to ensure that payroll time sheets submitted by contractors and subcontractors are reviewed to verify that information provided on job calculator forms is complete and accurate.

## Conclusion

The Agency generally administered its Program in accordance with the Recovery Act and HUD requirements. However, although the audit disclosed no material deficiencies with the Agency's Program, the Agency needs to address the ineligible and unsupported costs identified by the audit, obtain lobbying certifications from contractors and subcontractors as required, and improve its process for reporting job creation information to the Federal reporting Web site.

## Recommendations

We recommend that the Director of the Office of Affordable Housing Programs require the Agency to

- 1A. Reimburse its Program \$135,590 from non-Federal funds for the ineligible costs identified by the audit.
- 1B. Provide documentation to support the \$151,936 in unsupported costs identified by the audit or reimburse its Program from non-Federal funds for any costs that it cannot support.
- 1C. Obtain and review the required lobbying certifications from contractors and subcontractors.
- 1D. Develop and implement controls to ensure that accurate job information is reported on the Federal reporting Web site.

## SCOPE AND METHODOLOGY

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We conducted the audit from May through September 2010 at the Agency's office located at 211 North Front Street, Harrisburg, PA, and our office located in Philadelphia, PA. The audit covered the period February 2009 through May 2010 but was expanded when necessary to include other periods. We relied in part on computer-processed data in the Agency's computer system. Although we did not perform a detailed assessment of the reliability of the data, we did perform a minimal level of testing and found the data to be adequate for our purposes.

To accomplish our objective, we reviewed

- Relevant background information.
- The Recovery Act.
- Section 42 of the Internal Revenue Code pertaining to the LIHTC program.
- Program guidance found on HUD's Web site. The reference material included information on requirements for written agreements, the National Environmental Policy Act, lead-based paint, and program income.
- The Program agreement between HUD and the Agency, dated June 26, 2009, and documents related to the Program application submitted by the Agency to HUD before the execution of the Program agreement.
- Correspondence prepared by HUD, the Agency, and other related parties receiving Program funds.
- The Agency's policies and procedures related to financial reporting, general payout procedures, monitoring, and program guidelines related to Recovery Act funds and LIHTC.
- The Agency's organizational chart, an employee listing, and its standards of conduct for its employees.
- The Agency's policies and procedures related to the LIHTC program.
- The Agency's audited financial statements for the periods ending June 30, 2008, and June 30, 2009.
- The Agency's Recovery Act Web site.

- Program funding provided to 28 projects, including other sources of funds used to finance the construction or rehabilitation of the properties.
- Program agreements between the Agency and the project owners for the 26 projects for which the Agency had committed Program funds as of February 16, 2010.
- Job calculator forms for the period ending June 30, 2010, and weekly payroll information submitted by the contractors and subcontractors for two projects.

We nonstatistically selected 5 of the 28 projects that were awarded Program funds as of July 4, 2010, to determine whether the costs were eligible and properly supported. The five projects were awarded a total of \$22.7 million in Program funds of the \$95.1 million the Agency received. The amount of Program funds awarded to these five projects ranged from \$492,000 to \$7.6 million. The sample of five projects consisted of the projects with the three largest Program grants and the projects with the two smallest Program grants. As of July 4, 2010, the Agency had disbursed \$36.1 million in Program funds, of which \$9.7 million was disbursed to these five projects.

We visited two of the five sample projects to observe the work progress.

We interviewed relevant Agency staff and officials from HUD's Office of Affordable Housing Programs, and Office of Community Planning and Development, Philadelphia Regional Office.

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

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Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

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

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## Relevant Internal Controls

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

- Policies, procedures, and other management controls implemented to ensure that the Agency administered Program funds in accordance with the Recovery Act and HUD requirements.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

We evaluated internal controls related to the audit objective in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance regarding the effectiveness of the internal control structure as a whole. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control.

## APPENDIXES

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### Appendix A

#### SCHEDULE OF QUESTIONED COSTS

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Recommendation number	Ineligible 1/	Unsupported 2/
1A	\$135,590	
1B		\$151,936

- 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



Brian A. Hudson, Sr.  
*Executive Director & CEO*

October 21, 2010

John P. Buck  
Regional Inspector General for Audit,  
Department of Housing and Urban  
Development  
Wanamaker Building  
100 Penn Square East, Suite 10205  
Philadelphia, PA 19107-3380

Re: Pennsylvania Housing Finance Agency Audit Report  
Tax Credit Assistance Program

Dear Mr. Buck:

The Agency is in receipt of the draft Audit Report prepared in connection with the Pennsylvania Housing Finance Agency's ("PHFA") administration of the Tax Credit Assistance Program. We are delighted that the audit has substantially and materially confirmed our successful administration and allocation of funds from this valuable source, given that we have rapidly and efficiently deployed over \$95,000,000 in funding to fund more than 1,300 units of affordable housing in Pennsylvania. We provide the following written comments to the draft report.

**Finding 1A** - Reimburse its Program \$135,590 from non-Federal funds for the ineligible costs identified by the audit.

It is our understanding that the costs related to this item were related to three expenditures. The first relates to TCAP funds expended for municipal improvements in the amount of \$107,123. The Agency had determined that these costs were to be treated as municipal fees. Upon further review, the Agency acknowledges that these costs were in fact escrowed by the municipality. It is our understanding that the improvements have been made and will document this or will reimburse the funds accordingly. The funds expended for the remaining identified expenditures will be reimbursed with non-Federal funds.

**Finding 1B** - Provide documentation to support the \$151,936 in unsupported costs identified by the audit or reimburse its Program from non-federal funds for any costs that it cannot support.

These costs were related to legal fees incurred in connection with the development of Oak Hill Apartments. The Agency believes it received sufficient back-up to demonstrate that these costs are TCAP eligible. The Agency will provide additional documentation to further substantiate their eligibility.

**Finding 1C** - Obtain and review the required lobbying certifications from contractors and subcontractors.

The Agency has established a process to secure these certifications.

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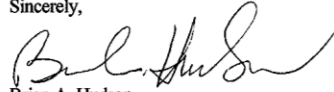
[www.phfa.org](http://www.phfa.org)  
[bhudson@phfa.org](mailto:bhudson@phfa.org)

**Finding 1D** – Develop and implement controls to ensure that accurate job information is reported on the Federal reporting Web site.

The Federal reporting Web site (Section 1512 report) captures job creation information on a quarterly basis. The Agency must submit the report by the 10<sup>th</sup> day of the month following the end of a quarter. Due to the fact that payroll information is supplied to the Agency based on weekly payrolls and this information may not be submitted during the same time period that the Section 1512 report must be entered on the Web site, the data may not match on a quarterly basis. However, cumulative data collected should reflect accurate job counting. The process in which the Agency collects this data has been modified to ensure that the cumulative job data will be reported.

Thank you for this opportunity to respond to the minor, but important, inconsistencies noted in your report. We will address as noted. If you have any questions, please contact me.

Sincerely,



Brian A. Hudson  
Executive Director