



Issue Date	January 25, 2011
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Audit Report Number	2011-FW-1005
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TO: Dan Rodriguez, Director, Office of Public Housing, 6EPH

FROM: *//signed//*  
Gerald R. Kirkland  
Regional Inspector General for Audit, Fort Worth Region, 6AGA

SUBJECT: The Housing Authority of the City of Port Arthur, TX, Mismanaged Its  
Recovery Act Funding

## **HIGHLIGHTS**

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

In accordance with our goal to review funds provided under the American Recovery and Reinvestment Act of 2009 (Recovery Act), we audited the Housing Authority of the City of Port Arthur's (Authority) Public Housing Capital Fund Stimulus (formula) Recovery Act Funded activities. We wanted to determine whether (1) Public Housing Capital Fund formula grant obligations made between January 30 and March 17, 2010, were appropriate, prudent, eligible, and supported and (2) related procurements were made in accordance with 24 CFR (Code of Federal Regulations) Part 85 and Recovery Act requirements. Additionally, we assessed the Authority's compliance with Recovery Act reporting and environmental review requirements.

### **What We Found**

The Authority's Recovery Act obligation was not appropriate, prudent, eligible, and supported because its related procurement was not made in accordance with 24 CFR Part 85 and Recovery Act requirements. The Authority violated procurement requirements designed to ensure full and open competition and reasonable cost and did not practice sound financial controls over the grant. As a

result, the Authority's obligation of its \$725,546 Recovery Act grant and its resulting expenditures were ineligible. In addition, the Authority did not comply with Recovery Act environmental review reporting requirements and it commenced site work for its project before receiving environmental clearance to proceed.

### **What We Recommend**

We recommend that the U. S. Department of Housing and Urban Development (HUD) rescind the Authority's Recovery Act grant, including the \$67,640 expended, and return the entire \$725,546 allocation to the U. S. Treasury. HUD should also ensure that the Authority complies with procurement requirements, adopts adequate financial controls, and complies with environmental review requirements. We further recommend that HUD prohibit the Authority from conducting further site work until it receives environmental clearance to do so, regardless of the funding source.

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 issued a draft report to the Authority and HUD on December 21, 2010, and requested written comments by January 12, 2011. We conducted an exit conference on January 6, 2011. The Authority requested an extension of time to provide written comments and provided them on January 19, 2011. The Authority generally disagreed with the report. We made some revisions to the report language based on the Authority's comments but did not revise the overall conclusions and recommendations. 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

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The Housing Authority of the City of Port Arthur (Authority) is a public body, both corporate and politic, that was established pursuant to the laws of the State of Texas for the purpose of engaging in the development, acquisition, and administration of a low-income housing program. The governing body of the Authority is its board of commissioners. The Authority is fiscally independent of the City of Port Arthur (City) and is not considered a component unit of the City.

The Authority receives capital funds annually via a formula from the U. S. Department of Housing and Urban Development (HUD). The Authority may use its capital funds for development, financing, modernization, and management improvements for its public housing developments. It received \$573,191 and \$582,663 in formula capital funds in 2008 and 2009, respectively.

On February 17, 2009, the President signed the American Recovery and Reinvestment Act of 2009 (Recovery Act) into law.<sup>1</sup> The Recovery Act provided \$4 billion for public housing agencies to carry out capital and management activities, including modernization and development of public housing. It allocated \$3 billion for formula grants and \$1 billion for competitive grants. The Recovery Act required public housing agencies to obligate 100 percent of the funds within 1 year of the date on which funds became available to the agency for obligation and expend 60 percent within 2 years and 100 percent within 3 years of such date.

HUD allocated \$725,546 to the Authority for its Recovery Act Public Housing Capital Fund formula grant (formula grant). HUD made the formula grant available to the Authority on March 18, 2009, resulting in a statutory obligation deadline of March 17, 2010. If the Authority failed to comply with the obligation deadline, the Recovery Act required HUD to recapture all remaining unobligated funds and reallocate them to agencies that complied with those requirements.<sup>2</sup>

HUD required the Authority to use its Recovery Act grant on eligible activities already identified in either its annual statement or Five-Year Action Plan (action plan).<sup>3</sup> The HUD-approved comprehensive plan sets forth all of the Authority's physical and management improvement needs for its public housing developments and must demonstrate long-term physical and social viability of proposed projects, including cost reasonableness. If the Authority decided to undertake work items not in its approved plans, HUD required it to amend its approved plans.

Our audit objectives were to determine whether obligations the Authority made between January 30 and March 17, 2010, were appropriate, prudent, eligible, and supported and procurements were made in accordance with requirements and to assess the Authority's compliance with Recovery Act reporting and environmental review requirements.

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<sup>1</sup> Public Law 111-5

<sup>2</sup> The Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111-203) amended the Recovery Act, requiring recaptured funds to be returned to the U. S. Treasury and dedicated for the sole purpose of deficit reduction.

<sup>3</sup> The annual statement, annual plan, and action plan were all components of the Authority's comprehensive plan.

## RESULTS OF AUDIT

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### Finding: The Authority Mismanaged Its Recovery Act Funding

The Authority poorly planned its Recovery Act activities, violated procurement regulations and Recovery Act requirements, did not practice sound financial controls, failed to meet reporting requirements, and commenced site work for its project before receiving environmental clearance to proceed. In its haste to meet strict Recovery Act obligation and expenditure deadlines, the Authority disregarded these requirements. As a result, it committed its \$725,546 Recovery Act grant without ensuring it obtained goods and services at a reasonable cost for a prudently planned project.

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#### The Authority Poorly Planned Its Recovery Act Activities

The Recovery Act required the Authority to give priority consideration to the rehabilitation of vacant rental units, prioritize capital projects that were already underway or included in its action plan, and give priority to capital projects that could award contracts based on bids within 120 days from the date the funds were made available.<sup>4</sup>

For the first 8½ months of the grant, the Authority considered using its Recovery Act grant as part of a complex mixed-finance redevelopment project for its Carver Terrace public housing development, with the hope of leveraging funds that were not available at the time. It anticipated receiving disaster recovery funds from the State of Texas that it could use in conjunction with the Recovery Act grant for this purpose, including acquiring land to use for replacement housing for Carver Terrace, which was damaged by Hurricane Rita in 2005. The Authority's original grant budget allocated the funds mainly for site acquisition, as shown in table 1.

**Table 1:** Initial Recovery Act grant budget, dated April 7, 2009

Budget line item	Description	Amount
1430/Fees and costs	Architects, engineering, and environmental	\$50,000
1440/Site acquisition	Site acquisition	600,546
1470/Non-dwelling structures	Educational computer & activity building	75,000
	<b>Total</b>	<b>\$725,546</b>

When it became clear to the Authority that the disaster recovery funds would not be available in time to obligate its Recovery Act grant before the deadline, it decided to change its plans. With about 3½ months remaining before the obligation deadline, the Authority amended its action plan on December 3, 2009, to add a learning center

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<sup>4</sup> HUD made funds available on March 18, 2009. The 120-day award period would have been through July 16, 2009. The Authority did not enter into an agreement until December 2009.

at its Gulfbreeze Place public housing development.<sup>5</sup> The Authority stated it had wanted to construct a learning center at Gulfbreeze Place for some time, but it had not previously included this item in its action plan. As shown in table 1, the Authority included the learning center in its initial grant budget even though it was not part of its approved action plan at the time. However, the Authority did amend its action plan before entering into a contract to obligate the funds and complied with the related public notice requirements.

The Authority revised its grant budget in its amended action plan to allocate the grant funds as shown in table 2. At that time, it was still not clear how much it planned to spend on the learning center project, as it included three distinctly different projects in the same category in its budget (non-dwelling structures).

**Table 2:** Recovery Act grant budget in revised action plan, dated December 3, 2009

<b>Budget line item</b>	<b>Description</b>	<b>Amount</b>
1410/Administration	Administration	\$72,000
1430/Fees and costs	Architects, engineering, and environmental	100,000
1440/Site acquisition	Site acquisition	100,000
1470/Non-dwelling structures	Educational computer and activity building/administration office/ replacement housing	453,546
	<b>Total</b>	\$725,546

The Authority's action plan did not include an estimate of what it would cost to operate the facility but did include a list of potential sources of funds to operate this and another newly proposed initiative as follows:

Funding for these initiatives may come from a variety of sources: the Port Arthur Housing Authority, the City, the City's Economic Development Commission, Regional Planning Commission, the State, Federal and private resources.

This statement further demonstrated the Authority's failure to adequately plan how it would undertake and fund the projects it proposed for its community.

The Authority believed it had limited options to spend its grant funds. It had demolished and rebuilt Gulfbreeze Place in 2008-2009, with occupancy beginning in March 2010. Therefore, that development did not require rehabilitation. Because the Authority planned to seek approval from HUD to demolish the units at Carver Terrace and redevelop replacement units elsewhere, the executive director believed it would be imprudent to use Recovery Act funds to rehabilitate that property. However, the Authority should have had viable options in its existing action plan for spending the funds, as it was required to plan in advance how it would spend its annual capital fund allotment of more than \$500,000 over a 5-year period. Further,

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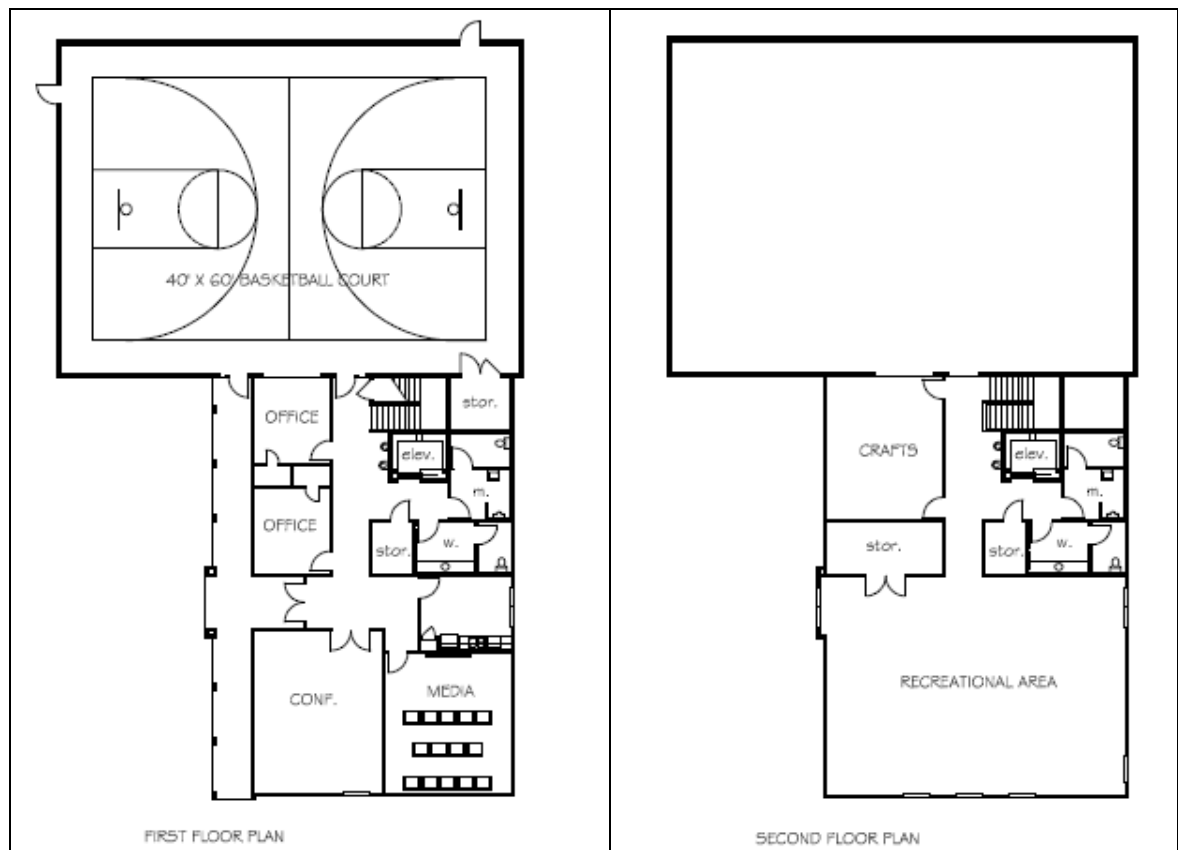
<sup>5</sup> The development has been called Gulf Breeze Plaza, Gulfbreeze Place, Gulfbreeze I, and Lakeview Palms on various documents.

by amending its plan to add a new project, the Authority did not prioritize capital projects that were already planned or underway as directed by the Recovery Act.

### The Project Already Had Some of the Amenities Planned for the Learning Center

The new development at Gulfbreeze Place had 86 units of public housing and a leasing center, which included a kitchen, computer room, lounge area, and fitness center. The preliminary specifications for the Authority's proposed learning center<sup>6</sup> on a parcel of land adjacent to Gulfbreeze Place called for a two-story building comprised predominantly of a 40-by-60-foot indoor basketball court. The design also included offices, a conference room, and a media room with computers on the first floor and a craft room and recreational area on the second floor (refer to figure 1). While the learning center may have been considered an eligible use of capital funds, some of the proposed amenities were similar to amenities in the newly constructed leasing center.

**Figure 1:** Preliminary diagram of learning center as of January 2010



<sup>6</sup> The Authority has also referred to the project as a tenant services building. In its reports on Recovery.gov, the Authority published that it was building an “Educational Computer Activity Building at our Public Housing Apartments.”

## **The Authority Violated Procurement Regulations**

HUD specifically instructed grantees to comply with Federal procurement requirements in 24 CFR (Code of Federal Regulations) Part 85 and allowed them to follow the guidance in its Procurement Handbook for Public Housing Agencies.<sup>7</sup> However, the Authority disregarded these requirements when it entered into a noncompetitive agreement to obligate its grant funds, neglected to perform the required independent cost estimate, and failed to maintain records sufficient to detail the significant history of the procurement. The Authority also had a history of procurement-related noncompliance issues but had not corrected them.

### **The Authority Awarded the Contract without Competition or Justification**

The Authority entered into a development agreement effective June 2008 for the demolition and reconstruction of Gulfbreeze Place. Rather than follow competitive bidding requirements, the Authority executed an addendum to the development agreement, effective December 15, 2009, to add a learning center/tenant services building on a parcel of land adjacent to Gulfbreeze Place. It rationalized that the addendum was part of the original development agreement the board had approved. However, the fact that the Authority recognized the need to execute an addendum to add the learning center to the development agreement indicated it was not part of the existing agreement. The Authority believed it was appropriate to award the work directly to the same developer because the development was new and it knew the developer and was pleased with the developer's work.

The Authority provided no evidence the learning center was intended as part of the original development agreement. A learning center was not marked on the list of amenities to be provided when it planned the redevelopment project in 2007, even though the Amenities form included options for "Furnished and staffed Children's Activity Center" and "Sport Court (Tennis, Basketball or Volleyball)."<sup>8</sup> As shown in appendixes C and D, the land on which the Authority planned to build the learning center was not included in the original redevelopment project. Site plans for Gulfbreeze Place did not include the learning center or the land until 2010, when the architect prepared plans showing how it would incorporate the learning center into the existing development.

Because the new building was beyond the scope of the original development contract, HUD's policy considered this a major change and required a new

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<sup>7</sup> Office of Public and Indian Housing (PIH) Notice PIH 2009-12 (HA), issued March 18, 2009

<sup>8</sup> Source: The Authority's Texas Department of Housing and Community Affairs 2007 Multifamily Uniform Application for Community Development Block Grant (CDBG) Disaster Recovery funds for Gulfbreeze Plaza I & II



procurement.<sup>9</sup> The Authority violated this requirement when it awarded the work without competition to its existing developer.

Federal procurement regulations allowed the Authority to award contracts by soliciting noncompetitive proposals from only one source in certain situations, including a public exigency or emergency.<sup>10</sup> HUD's Recovery Act procurement guidance<sup>11</sup> gave grantees the latitude to use the public exigency exception to justify noncompetitive awards based on the Recovery Act requirement to commence expenditures and activities as quickly as possible. HUD cautioned grantees that they must comply with all procurement requirements, including the requirement for a cost analysis, the conflict-of-interest requirement, and the requirement to maintain records sufficient to detail the significant history of each contract's procurement. The Authority failed to document its justification for the noncompetitive award. In fact, there was no evidence the Authority solicited or evaluated a proposal from the developer; it merely added the learning center to the existing development agreement.

### **The Authority Neglected to Perform an Independent Cost Estimate for the Project**

The Authority did not perform an independent cost estimate before entering into the agreement, as required by Federal regulations. The executive director and a consultant stated they discussed whether they could construct the desired building with the available Recovery Act funds, and the consultant stated the Authority could not perform a cost estimate without preliminary drawings, which it did not have at the time it entered into the agreement with the developer. As a result, the Authority haphazardly assigned costs to the project at various points in time. As shown in table 3, it assigned costs to the project ranging from \$75,000 to more than \$1.3 million. Further, the Authority accepted an arbitrary budget of \$750,000 proposed by the developer when it had allocated only \$453,546<sup>12</sup> of its Recovery Act grant for this and two other projects.

In October 2010, the Authority used the developer's engineering diagrams and design specifications to obtain a cost analysis for the project from a consultant, which estimated a reasonable budget for the project would be more than \$1.3 million. Clearly, the Authority failed to adequately budget for the project and allowed its developer to steer cost via its design specifications. It is unclear whether or how the Authority planned to fund any budget shortfall. Further, the Authority had not identified a source of funds to cover the facility's operating costs.

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<sup>9</sup> HUD Handbook 7460.8, REV-2, Procurement Handbook for Public Housing Agencies, dated February 2007, section 11.4.C

<sup>10</sup> 24 CFR 85.36(d)(4)

<sup>11</sup> Notice PIH 2009-12 (HA), issued March 18, 2009

<sup>12</sup> The Authority allocated another \$100,000 of its Recovery Act grant for unspecified fees and costs, some of which presumably related to the learning center project.

**Table 3:** Changes in project budget over time

Date	Budget/cost document	Project budget
4/7/2009	Initial grant budget	\$75,000
12/3/2009	Revised grant budget	453,546
12/15/2009	Development agreement addendum	750,000
10/21/2010	Consultant's cost analysis	1,314,848
	Variance (highest vs. lowest)	\$1,239,848

### **The Authority Kept Inadequate Procurement Records**

The Authority did not have a system of records that allowed it to demonstrate the significant history of the procurement. It did not maintain consolidated procurement records for its contracts, including the rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

Since the agreement for the Recovery Act work was an addendum to an existing contract, it was necessary to review the original procurement records.<sup>13</sup> After searching the Authority's administrative offices and an offsite storage warehouse, the Authority was unable to produce the bids it received in response to its original request for proposals and qualifications. The Authority later provided copies of its bid evaluation and scoring forms, but not the bids themselves.

### **The Authority Had a History of Procurement Issues**

The Authority had written procurement policies that it obtained from a consultant and were consistent with Federal procurement requirements. However, as described above, there was no evidence the Authority followed its policy or valued the underlying concepts of full and open competition or cost reasonableness. The Authority's fiscal year 2008 financial statement audit report included two procurement-related findings. The Authority

- Did not maintain documentation for procurement transactions in accordance with requirements, including incomplete bid tabulations, lack of support for quotes obtained, and its rationale for the method of procurement.
- Did not include required prevailing wage rate clauses in construction contracts, and there was no evidence of required contractor-submitted weekly certified payrolls in the Authority's records.

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<sup>13</sup> The original solicitation was for qualifications and proposals to redevelop Gulfbreeze Place and other public housing using the Texas Department of Housing Community Affairs Community Development Block Grant Disaster Recovery program and at the sole option of the Authority to develop possible additional affordable housing developments using this program, low-income housing tax credits, and/or other financing. Proposals were due June 25, 2007. This solicitation suggested the Authority had preselected awardees, as evidenced by language in the solicitation: "All properties had hurricane damages and insurance claims were filed. Copies of the insurance claims were faxed to you."

In its corrective action plan included in its 2008 audit report, the Authority asserted it had implemented procedures to correct the deficiencies. Contrary to this assertion, it had not, as evidenced by its mismanagement of its Recovery Act grant. Further, the Authority's fiscal year 2009 audit report repeated the finding related to prevailing wage rates. Again, the Authority promised to implement procedures to ensure it complied with the requirement. HUD staff also commented that procurement continued to be an issue at the Authority. The executive director acknowledged the previous audit findings and the need to maintain adequate documentation. He recognized the Authority's vulnerability in this area but had not taken definitive steps to improve its procurement function.

Because the Authority did not follow procurement requirements, it committed its \$725,546 Recovery Act grant without ensuring it obtained goods and services at a reasonable cost for a prudent project. Further, the \$67,640 the Authority expended on fees and costs (see below) was ineligible. HUD should rescind the Authority's Recovery Act formula grant, require it to repay the \$67,640 already expended, and return the entire \$725,546 to the U.S. Treasury for the sole purpose of deficit reduction.

### **The Authority Did Not Practice Sound Financial Controls**

For its Recovery Act expenditures, the Authority did not exhibit basic financial controls, such as separation of duties between those authorizing payments and those requesting the goods or services or ensuring it paid expenses in a timely manner. It had no formal procedures for invoice review and approval or for ensuring it charged expenses to the correct source. The executive director was heavily involved in procurement, the receipt and approval of invoices, and cost allocation. He also signed the checks, as did a board member.

As of October 31, 2010, the Authority had drawn down \$67,640 (9 percent) of its Recovery Act grant for fees and costs, supported by four invoices. Examination of the underlying invoices showed the Authority did not pay two of four invoices on time (refer to table 4) and did not properly authorize three of four payments. It paid one invoice more than 90 days after the invoice date, and documentation attached to a second invoice showed the vendor requested payment four times before the Authority paid it.

**Table 4:** Schedule of invoice payments

Invoice number	Invoice amount	Invoice date	Date paid	Authorization/ evidence of approval
4000-01	\$10,000	3/31/2010	5/18/2010	E-mail from executive director
AES095912	2,640	4/1/2010	7/2/2010	None
4000-02	30,000	7/1/2010	7/22/2010	Executive director's initials and "ARRA" <sup>14</sup> on invoice
4000-03	25,000	7/19/2010	7/22/2010	Executive director's initials and "ARRA" on invoice

While there was evidence the executive director directed the staff to pay three of the four invoices, they were not properly authorized. Specifically, the invoices contained no evidence or certification that the Authority received the goods and services billed. However, auditors were able to trace the expenses to the specific deliverables, which included an environmental site assessment, an architectural agreement, and architectural plans. Further, there was a lack of separation of duties between the authorization of payments and the requesting of goods and services, as the executive director both procured all the invoiced services and approved the payments.

The Authority's fiscal year 2009 audit included two findings that the Authority did not have supporting documentation for vendor payments, including the lack of supervisor approval and discrepancies between the invoice amount and the amount paid. According to finance staff, the Authority did not follow formal policies and procedures for incoming invoices, including routing and approval. Staff explained that the executive director or the director of property services would hand an invoice for payment to the payables clerk and tell her what grant to charge for the expense. The executive director acknowledged the need to use purchase orders and ensure controls were in place but had not taken corrective action. The Authority should establish and implement procedures to ensure the proper routing and approval of invoices and adequate separation of duties between those requesting goods and services and those approving payments. This measure will help to ensure the Authority allocates costs to the appropriate source and that it receives the goods and services for which it pays.

### **The Authority Failed To Meet Reporting Requirements**

One of the central tenets of the Recovery Act was the concept of accountability and transparency. To this end, it required recipients to report funds received, expended, or obligated to projects or activities,<sup>15</sup> which would be reviewed by the awarding agency and then posted to the Web site Recovery.gov. The Authority was required to submit the reports within 10 days after the end of each calendar

<sup>14</sup> "ARRA" is a widely used acronym for the Recovery Act.

<sup>15</sup> Section 1512

quarter, beginning the third quarter of 2009. The Authority submitted the quarterly reports; however, it filed its first three reports late. In addition, the Authority used the incorrect grant number on its first report. It submitted its fourth quarterly report on time (refer to table 5).

The Recovery Act<sup>16</sup> also required that applicable environmental reviews under the National Environmental Policy Act (NEPA) be completed on an expeditious basis. HUD developed the Recovery Act Management Performance System (RAMPS) for Recovery Act grantees to use for reporting on environmental compliance and required the Authority to report NEPA compliance in RAMPS by October 10, 2009. It required quarterly reporting thereafter until the environmental reviews were completed for each activity funded with Recovery Act funds. HUD performed a monitoring review in November 2009 and gave the Authority an extension until January 15, 2010, to complete this process. However, as of August 2010, the Authority had not fulfilled its environmental reporting responsibility. On October 22, 2010, the Authority entered information into RAMPS stating that the environmental review was pending and it expected to complete the review on November 1, 2010.

**Table 5:** Recovery Act reporting submissions

<b>Report</b>	<b>Due date</b>	<b>Date submitted</b>	<b>Days late</b>
Q3 2009	10/10/2009	10/20/2009	10
Q4 2009	1/10/2010	1/14/2010	4
Q1 2010	4/10/2010	4/13/2010	3
Q2 2010	7/10/2010	7/9/2010	-
NEPA	1/15/2010	none	300+ <sup>17</sup>

### **The Authority Commenced Site Work without Environmental Clearance**

By signing the grant agreement, the Authority agreed to carry out its capital activities in accordance with all HUD regulations, including the environmental review requirements under 24 CFR Parts 50 and 58. Those regulations required the Authority to provide the City, as the responsible entity conducting the environmental review, with all available project and environmental information. The City was required to complete an environmental certification, which the Authority was required to submit to HUD with a request for release of funds. The Authority was required to refrain from undertaking any physical activities until HUD approved its request for release of funds.

The environmental review process should begin as soon as a recipient determines the projected use of HUD assistance. The Authority initiated this process in

<sup>16</sup> Section 1609

<sup>17</sup> As of December 3, 2010, the report was 322 days overdue.

November 2009 when it engaged a consultant to perform an environmental site assessment. The assessment revealed no onsite recognized environmental conditions in connection with the property but noted the property had previously been used as a gas station. The Authority later determined there were underground gas tanks on the property and in September 2010 had them removed, although the City had not completed the environmental certification and the Authority had not submitted the information to HUD.

It appeared the Authority was so determined to complete the project before the grant expenditure deadline<sup>18</sup> that it chose not to comply with rules designed to protect people and the environment. By disturbing the potentially contaminated site before receiving clearance to do so, the Authority exposed itself, the City, and HUD to potential liability.

## **Conclusion**

The Authority mismanaged its Recovery Act formula grant. It failed to adequately plan its use of the grant and disregarded fundamental requirements for procurement, finance, and environmental review that were designed to ensure full and open competition, reasonable cost, receipt of goods and services, and the protection of people and the environment. As these requirements are the overarching principles of Federal grant administration, we question the Authority's capacity to adequately operate its public housing programs.

## **Recommendations**

We recommend that the Director, Office of Public and Indian Housing,

- 1A. Rescind the Authority's \$725,546 Recovery Act grant and return the funds to the U. S. Treasury in accordance with the Recovery Act, as amended, for the sole purpose of deficit reduction. This amount includes the \$67,640 already expended and the balance of \$657,906.
- 1B. Require the Authority to implement procedures to ensure it complies with all relevant procurement requirements. This process may include the provision of technical assistance on HUD's part.
- 1C. Require the Authority to adopt and implement financial controls to ensure the proper routing and approval of invoices and adequate separation of duties between those requesting goods and services and those approving payments.

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<sup>18</sup> The Authority was required to expend 60 percent of the grant before March 17, 2011.

- 1D. Provide the Authority with or require it to obtain training on environmental review requirements.
- 1E. Prohibit the Authority from conducting further activity on the site of the proposed learning center until it receives environmental clearance to do so, regardless of the funding source.

## SCOPE AND METHODOLOGY

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The scope of the review was the Authority's Recovery Act Public Housing Capital Fund formula grant obligations made between January 30 and March 17, 2010. The Authority obligated its entire grant during this period, so we reviewed activities related to the obligation and expenditure of the grant funds, which generally took place between March 2009 and November 2010. We performed the work at the Authority's administrative offices in Port Arthur, TX, and our offices in Fort Worth, TX, from August 4 through December 3, 2010.

To accomplish our objectives, we performed the following steps as they related to the Authority's Recovery Act Public Housing Capital Fund formula grant:

- Reviewed relevant laws, regulations, and HUD guidance.
- Reviewed meeting minutes of the Authority's board of commissioners.
- Reviewed the Authority's audited financial statements for fiscal years 2008 and 2009.
- Reviewed the Authority's Recovery Act Public Housing Capital Fund formula grant agreement, procurement policies, revised action plan, procurement records, invoice payments and related deliverables, status reports, and environmental review reporting.
- Assisted the Authority in searching for procurement records at an offsite storage facility.
- Conducted site visits of and photographed the Authority's Gulfbreeze Place public housing development and the adjacent site of the proposed learning center.
- Obtained a legal opinion concerning whether the learning center was an eligible use of Recovery Act capital funds.
- Interviewed the Authority's staff, its consultant, and HUD staff in Houston and Fort Worth, TX, and Washington, DC.

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

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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 objectives:

- Controls to ensure the Authority followed procurement requirements.
- Controls to ensure payments were properly authorized and allocated to the appropriate source and that the Authority received the goods and services for which it paid.
- Controls to ensure the Authority met mandated environmental review requirements.

We assessed the relevant controls identified above.

A deficiency in internal controls 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.

## Significant Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The Authority did not have a system in place to ensure it followed its procurement policies or documented its procurement activities (finding).

- The Authority did not have procedures in place to ensure invoice payments were properly authorized and allocated and that the Authority received the goods or services for which it paid (finding).
- The Authority lacked controls to ensure it received environmental clearance before commencing construction activities (finding).

## APPENDIXES

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### Appendix A

#### SCHEDULE OF QUESTIONED COSTS

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Recommendation number	Ineligible <u>1/</u>
1A	\$725,546

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.

## Appendix B

### AUDITEE COMMENTS AND OIG'S EVALUATION

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#### Ref to OIG Evaluation

#### Auditee Comments



**COMMISSIONERS**  
REV. RONNIE LINDEN, CHAIRMAN  
DESIREE EDWARDS, VICE-CHAIRMAN  
CLONIE AMBROISE  
BART BRAGG  
FARHANA SWATI

**EXECUTIVE DIRECTOR**  
CELE QUESADA

January 19, 2011

#### VIA FEDERAL EXPRESS AND E-MAIL

Mr. Gerald R. Kirkland, Regional Inspector General for Audit  
U.S. Department of Housing and Urban Development  
Office of Inspector General, Region VI  
819 Taylor Street, Suite 13A09  
Fort Worth, TX 76102

**RE: Management Comments to Discussion Draft Audit Report 2010-\_\_ - \_\_\_\_  
(Recovery Act Funding)**

Dear Mr. Kirkland:

On behalf of the Housing Authority of the City of Port Arthur, Texas (the "**Authority**"), I am writing to provide the Authority's comments to the discussion draft audit report ("**Report**") from the Office of Inspector General (the "**OIG**") relating to the Authority's management of funds (the "**ARRA funds**") provided under the American Recovery and Reinvestment Act of 2009 (the "**Recovery Act**"). The ostensible objective of the audit was to determine whether the Authority managed its ARRA funds in accordance with both the U.S. Department of Housing and Urban Development's ("**HUD**") requirements and the Recovery Act. In spite of this stated objective, substantial portions of the Report – particularly the sections addressing the Authority's "history of procurement issues" - focus on issues unrelated to the Authority's management of ARRA funds.

With the foregoing rationale in mind, the following are our comments on each of the findings and recommendations:

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**Comment 1**

**Finding 1: The Authority Mismanaged Its Recovery Act Funding**

**The Authority Poorly Planned Its Recovery Act Activities**

**Comment 2**

Authority's Response: Disagree. The Authority utilized a rational, businesslike approach in planning its use of the ARRA funds. Initially, the Authority determined that the best use of the ARRA funds, in conjunction with disaster assistance funds from the State of Texas and other monies, was to rehabilitate or replace the units at Carver Terrace. The State of Texas for disaster recovery fund deadlines and the Recovery Act expenditure deadlines made proceeding with Carver Terrace infeasible. Thus, the Authority acted prudently and responsibly to plan to use the ARRA funds for a different project. As the Report notes, the Authority properly amended its action plan and then executed an addendum to the Development Agreement in order to use the ARRA funds to develop a learning center at the Gulfbreeze Place housing development which was, at that time, under construction. Use of the funds at Gulfbreeze is certainly a "viable option" for the expenditure of the funds. In fact, the learning center had been on the agenda by the Authority's Board of Commissioners ("**Board**") for years prior to the ARRA funds becoming available.

**Comment 3**

**Comment 4**

The Report incorrectly portrays the Authority as failing to plan how it would financially undertake the operation of the learning center. The Report then sets forth the list of possible funding sources the Authority included in its plan to fund ongoing operational costs. In other words, the Report both criticizes the failure to plan and highlights the planning itself. In fact, it is premature to find fault with the Authority for not lining up funding which is not yet needed (while acknowledging that sources exist). The Authority will certainly pursue all available funding that may be available to provide services to its residents. Moreover, the Authority intends to operate the learning center as part of the overall Gulf Breeze development. As such, the costs and the reserves will be set forth in the annual operating budget as a whole rather than in a piece-meal fashion covering only a part of the overall development.

**The Proposed Learning Center Duplicated Some Existing Amenities at Gulfbreeze Place**

**Comment 5**

Authority's Response: Disagree. Fundamentally, the learning center amenities are intended to supplement, not duplicate the amenities in the leasing center. For example, while there is a fitness center in the leasing center, it does not include a full basketball court such as the one proposed in the learning center. The media room is intended to be used for different purposes, and will include different equipment than the computer room in the leasing center.

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Moreover, the Authority and its Board determined that the learning center was needed for the community. It was approved by HUD. It is not for the OIG to substitute its judgment as to what is needed in Port Arthur for that of the Board residing in Port Arthur.

As the Report accurately states, the learning center is an eligible use of capital funds.

**The Authority Violated Procurement Regulations In That It:**

- 1. Awarded the contract without competition or justification; and**
- 2. Neglected to perform an independent cost estimate for the project; and**
- 3. Kept inadequate procurement records.**

**Comment 6**

Authority's Response: Disagree. The Authority maintains that the new building was not beyond the scope of the original contract. The original scope of work contemplated the redevelopment of the Gulfbreeze site "in as entrepreneurial a manner as possible," and included, but was by no means limited to, the construction of public housing units. In fact, the Request for Qualifications ("RFQ") stated that offices and community space were to be developed. Accordingly, the addition of the learning center to the project necessitated only an amendment to the Development Agreement, not an entirely new procurement. Further, the learning center is not on "adjacent property" consisting of an otherwise separate site. The land for the learning center is part of the public housing development and has been since it was acquired in 1993.

**Comment 7**

As the Authority noted in the exit conference, the Authority has an independent cost estimate (which the Authority has referred to as a "cost analysis"), which was obtained as soon as the plans and specifications were completed. As the OIG is aware, the \$750,000 price on the Addendum to the Development Agreement was not intended as a not-to-exceed amount, but rather represented only the amount of ARRA funds that would be involved in the project.

**Comment 8**

With respect to procurement records, the Authority acknowledges that it can improve its record retention practices and procedures; however, the quote attributed to the Executive Director regarding the possibility that the bids were thrown away is taken grossly out of context. It was an off the cuff attempt at humor, and was not intended to be taken seriously. The RFQ, the response and the scoring have all been provided to the OIG.

**Comment 1**

The section of the Report addressing the Authority's "history of procurement issues" is inappropriate in the context of this audit, particularly when the OIG has not identified any material procurement problems, aside from document retention issues. Significantly, the

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Authority has engaged the services of Mike Gifford, a consultant specializing in procurement matters, to assist it in ensuring that all procurement requirements are fully met.

#### **The Authority Did Not Practice Sound Financial Controls**

#### **Comment 9**

Authority's Response: Disagree. This section raises issues regarding the payment of four particular invoices. Following the exit conference we believe that the OIG now concedes that three of the invoices at issue were paid properly. In particular, much of the delay in payment attributed to the Authority is actually due to the contractors' failure to submit appropriate invoices containing the requisite information to enable the Authority to process the payments. Had the Authority paid those invoices absent such documentation, that in and of itself would have appeared in the audit as a deficiency. With respect to the fourth invoice number AES095912 in the amount of \$2,640, the Authority acknowledges that it was paid both late and without sufficient evidence of approval. Consultant Mike Gifford is currently working with the Authority to develop a better system of procedures for invoice processing which will include checks and balances relating to purchasing and approval of invoices.

#### **The Authority Failed to Meet Reporting Requirements**

#### **Comment 10**

Authority's Response: Disagree. The Recovery Act report for the second quarter of 2010 was submitted on time. The first and fourth quarter Recovery Act reports were submitted three (3) and four (4) days late respectively. Only the third quarter Recovery Act report was submitted more than a week late, and the Authority notes that the Columbus Day holiday fell during that time. While the Authority acknowledges the importance of reporting deadlines, the deficiencies described in the Report are de minimus.

With respect to the NEPA reporting, the reporting could not be done until the site was cleared and the appropriate environmental approvals were received. Once the final environmental clearances were received, the NEPA reporting was entered on the Recovery Act Management and Performance System. Please also note that, as described in the following section, this was a second, unrequired, environmental clearance.

#### **The Authority Commenced Site Work Without Environmental Clearance**

#### **Comment 11 Comment 6**

Authority's Response: Disagree. The Report incorrectly stated the facts and then derived from them, improper conclusions. In fact, the Authority performed an environmental assessment on the entire site and obtained clearance from the Texas Department of Housing and Community Affairs ("TDHC") well before any work took place on the site. The work on the Gulf Breeze development began in 2007. At that time, the Authority resolved to revitalize an existing 152-unit complex comprised of 21 buildings into a new 86-unit multi-family residential community to be known as Gulf Breeze Plaza.

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**Comment 6**

**Comment 11**

The original Gulf Breeze Plaza apartments were constructed in 1955. Two adjacent lots were acquired in 1993 utilizing non-federal funds. The entire parcel was to be utilized for the revitalized Gulf Breeze development to include both residential units and related amenities. The Authority engaged Astex Environmental Services, Inc. to perform an environmental assessment pursuant to the requirements of 24 C.F.R. part 58.36. This environmental assessment was completed and delivered on December 21, 2007. The environmental assessment clearly set forth that capital funds, of which the ARRA funds are a part, would be utilized. Notice was properly posted and the clean environmental assessment was then submitted to the TDHC.

On March 21, 2008, the TDHC authorized the use of funds provided in granting the required compliance and approvals under 24 C.F.R. 58.36. TDHC further noted:

At combined a notice of a "finding of no significant impact" and of the intent/request for release of funds, affidavit of publishing and a request for release of funds certification (RROF) was submitted to HUD. After reviewing for accuracy and the conclusion of the 15-day federal comment period, HUD issued an authorization to use grant funds on 3-18-08.

**Comment 11**

**Comment 6**

Accordingly, on March 21, 2008, the Authority had completed an environmental assessment of the entire property and received all necessary compliance certificates from the local agency, as well as from HUD. This environmental review encompassed the entire Gulf Breeze property including the property now designated for the learning center.

**Comment 12**

Unfortunately, the Authority did not have sufficient funds to build out the total Gulf Breeze development. The learning center was thus postponed. Subsequently, the ARRA funds became available to the Authority and the Authority determined that the best use of funds was to proceed with a mixture of capital funds and ARRA funds to develop the learning center. While the Authority already had all of the necessary environmental clearances, it nonetheless did an additional review of the property. That review determined, for the first time, that underground storage tanks existed on the property. Based on this fact, the Authority acted in a prompt and responsible fashion and had the tanks removed. Once the tanks were removed, the Authority moved forward to obtain new clearance certificates from the City of Port Arthur. These were obtained on November 3, 2010.

As the foregoing clearly demonstrates, the Authority had all necessary environmental approvals. The environmental assessment of the entire site was completed on December 21, 2007 and the clearance certificates were issued by the Texas Department of Housing and Community Affairs on March 21, 2008. When underground storage tanks were subsequently discovered, the Authority acted in a responsible fashion in removing those tanks and only then sought additional clearance certificates for the property. Any other action would have been irresponsible. The fact remains that all proper documents were obtained and the Authority ensured a clean site.

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The following are the Authority's comments with respect to the individual recommendations set forth in the Report:

Recommendations

That the Director, Office of Public and Indian Housing:

*1A. Rescind the Authority's \$725,546 Recovery Act grant and return the funds to the U.S. Treasury in accordance with the Recovery Act, as amended, for the sole purpose of deficit reduction. This amount includes the \$67,640 already expended and the balance of \$657,906.*

Authority's Response: Disagree. As clearly set forth in the foregoing response, the Authority planned the use of the ARRA funds and procured a developer to develop the learning center on property which already had environmental clearance. Thus, no funds have been improperly committed or spent. Even if the Report's version of the facts were correct, the recommendation is premature, and belies both the fact that only \$67,640 has been expended thus far and that the Authority has until March 17, 2011 of this year to expend 60% of its ARRA funds. Working collaboratively with the HUD Field Office, the Authority would still have an opportunity to commit and to expend the remainder of its funds appropriately. Rescinding the Authority's entire grant would constitute an unjustified denial of the Authority's due process rights and ultimately simply serve to deprive the low income residents of Gulfbreeze Place of a learning center intended to benefit their entire community.

Rescinding the ARRA funds is not an appropriate remedy, especially where, as here, the Authority has properly proceeded with HUD's approval.

*1B. Require the Authority to implement procedures to ensure that it complies with all relevant procurement requirements. This process may include the provision of technical assistance on HUD's part.*

Authority's Response: Agree. The Authority is fully willing to comply with such requirements and has retained the services of Mike Gifford, a consultant specializing in procurement, to enable the agency to develop and to implement procedures that will help to bring the agency into full compliance with all procurement requirements.

*1C. Require the Authority to adopt and implement financial controls to ensure the proper routing and approval of invoices and adequate separation of duties between those requesting goods and services and those approving payments.*

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**Comment 13**

**Comment 14**

**Comment 14**

Authority's Response: Agree. The Authority is fully willing to adopt and to implement such controls and is willing to accept any training or technical assistance that HUD has to offer.

*ID. Provide the Authority with or require it to obtain training on environmental review requirements.*

**Comment 14**

Authority's Response: Although the Authority strenuously disagrees that it handled the environmental clearance incorrectly in this case, as outlined herein, the Authority is open to accepting any training that HUD wishes to provide.

*IE. Prohibit the Authority from conducting further activity on the site of the proposed learning center until it receives environmental clearance to do so, regardless of funding source.*

Authority's Response: Disagree. The Authority has the appropriate environmental clearance and there is no legitimate environmental impediment from continuing site work.

While the Authority agrees with certain findings in this discussion Report, we do not agree with all of them. Our hope is that you will reconsider both the finding and the numerous recommendations in light of these comments.

Very truly yours,

*//signed//*

Seledonio Quesada  
Executive Director

cc: Michael H. Syme, Esq.

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### **OIG Evaluation of Auditee Comments**

- Comment 1** The Authority took exception to our reporting its history of procurement issues as it was unrelated to its management of its Recovery Act funds. However, the Authority's history of procurement issues was relevant because it showed the Authority's continuing pattern of not complying with procurement requirements. We found procurement issues with the Recovery Act grant even after the Authority agreed to correct its prior deficiencies and asserted it had done so.
- Comment 2** The Authority believed it appropriately planned its use of the Recovery Act grant. We disagree. The Recovery Act's priorities for capital funds were rehabilitation of vacant rental units, capital projects already underway or included in the action plan, and projects that could award contracts within 120 days of the grant. None of the projects the Authority contemplated met these priorities. If the Authority had properly planned and procured the learning center, it would have been allowable.
- Comment 3** The Authority stated the learning center had been on the board agenda for years. However, the Authority provided no documentation supporting its claim. We reviewed the Authority's board meeting minutes from February 2009 through June 2010. Aside from approving the revised action plan, which included the learning center, during its December 3, 2009 meeting, there was no mention of the learning center in any of the board minutes we reviewed.
- Comment 4** The Authority argued it had adequately planned how it would operate the learning center, as it had listed possible funding sources in its action plan. Further, it stated it will set forth funds in its overall operating budget for the development. We disagree that listing entities from which it may receive funds was sufficient planning. Additionally, the Authority did not provide an operating budget that included the learning center and its comments indicated it had not developed one.
- Comment 5** The Authority disagreed that the amenities at the learning center duplicated amenities in the leasing center and stated we had substituted its judgment for that of the board. We agreed at the exit conference to revise the report language and have done so.
- Comment 6** The Authority maintained that the learning center was not beyond the scope of the original contract because its request for qualifications and proposals contemplated offices and community space. It also stated that the land for the learning center was part of the public housing development. However, the original redevelopment documents did not make reference to a learning center or similar project and both the legal description of the land and the land survey for the Gulfbreeze Place development excluded the adjacent lots in question (refer to appendixes C through E). For these reasons, we disagree that the learning center was part of the original development agreement and have revised the report language accordingly.

Regardless of the Authority's original plans, HUD's guidance specifically stated that adding the construction of a new building to a modernization contract would not be considered within the scope of the contract but should be considered a new contract and subject to competition. Since the learning center was not specifically in the development agreement, it required a new contract and cost estimate.

- Comment 7** The Authority was required to comply with federal procurement regulations, which clearly stated it must perform a cost or price analysis before receiving bids or proposals. None of the circumstances the Authority cited excused it from this requirement. The audit report accurately reflected that the Authority did not perform a cost estimate until 10 months after the effective date of the addendum to the development agreement.
- Comment 8** The Authority stated it had provided the request for qualifications and proposals (request), the response, and the scoring. It further stated OIG took the executive director's comment regarding record retention out of context. The Authority did provide the request and scoring sheets but did not provide the bids it received in response to the request. We removed the sentence regarding the executive director possibly throwing away the bids.
- Comment 9** The Authority stated we had agreed that three of four payments were paid properly. We agreed at the exit conference that it was difficult to determine from the documents when the contractor submitted an appropriate invoice for payment and agreed to revise the report language. However, after review of the related documents, we disagree that the payment was made in a timely manner in light of the contractor's repeated requests for payment. The documents provided did not show that the Authority told the contractor it had not received an appropriate invoice and would not pay until it received one.
- Comment 10** The Authority acknowledged the information in the report was correct but argued it was de minimus. The information was included in the report because it was indicative of the Authority's mismanagement and non-compliance with federal requirements. Regarding NEPA reporting, the Authority was prohibited from clearing the site until the environmental review was complete.
- Comment 11** The Authority asserted the parcel of land on which it planned to build the learning center was part of the 2007 environmental assessment for the overall Gulfbreeze development and that it received environmental clearance certificates for the "entire property." However, the Authority's documents contradicted its argument. The November 2009 environmental assessment of the land for the learning center was conducted by the same consultant as the 2007 assessment. The consultant's 2009 report stated that it was important to note that in December 2007, it conducted environmental assessments of the Gulfbreeze Place Apartments, but at that time the 0.468 acre of undeveloped land tract for the learning center was omitted; therefore, the current assessment was ordered as a supplement to the 2007 report. In addition, the original redevelopment

documents, including legal descriptions and land surveys, did not include this parcel of land in the project description (refer to appendixes C through E).

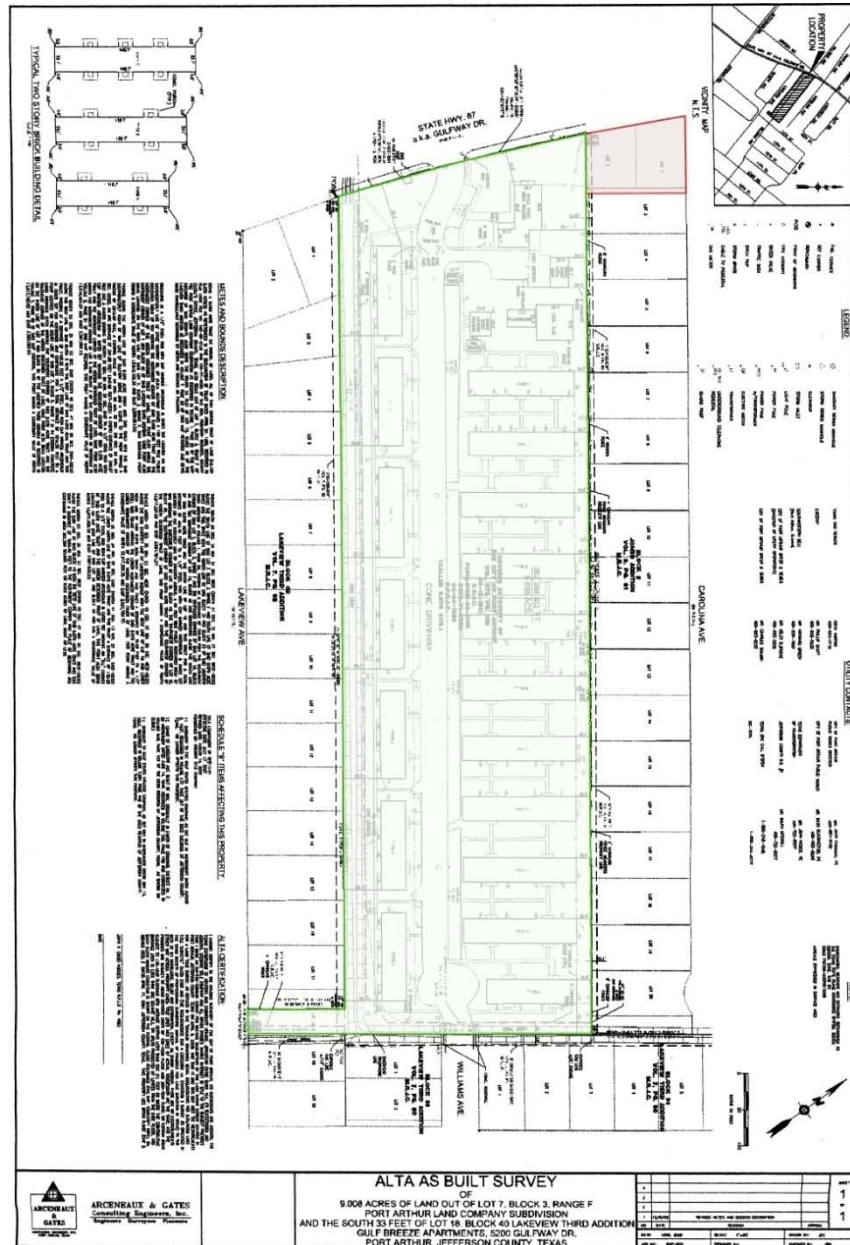
**Comment 12** The Authority stated the November 2009 environmental assessment identified the underground storage tanks on the property. This was incorrect; the assessment report stated the consultant found there was no visual evidence of any past underground tanks, fill ports, stained soils or other indications of past petroleum product use. The Authority later learned of the tanks when it began clearing the site in 2010, which was before it received environmental clearance from the City or HUD approval of its Request for Release of Funds. The Authority should not have cleared the site before receiving the requisite clearance. If it later found environmental problems (such as underground storage tanks), it would have been responsible for remediating them.

**Comment 13** The Authority argued the recommendation to rescind the grant was premature. However, because the Authority violated procurement requirements, its obligation of the Recovery Act grant was ineligible. The Recovery Act required HUD to recapture all funds not obligated by the 1-year deadline. Since the obligation was improper, HUD's only available remedy is to recapture the funds.

**Comment 14** The Authority agreed with recommendations 1B, 1C, and 1D. We acknowledge this agreement.

## Appendix C

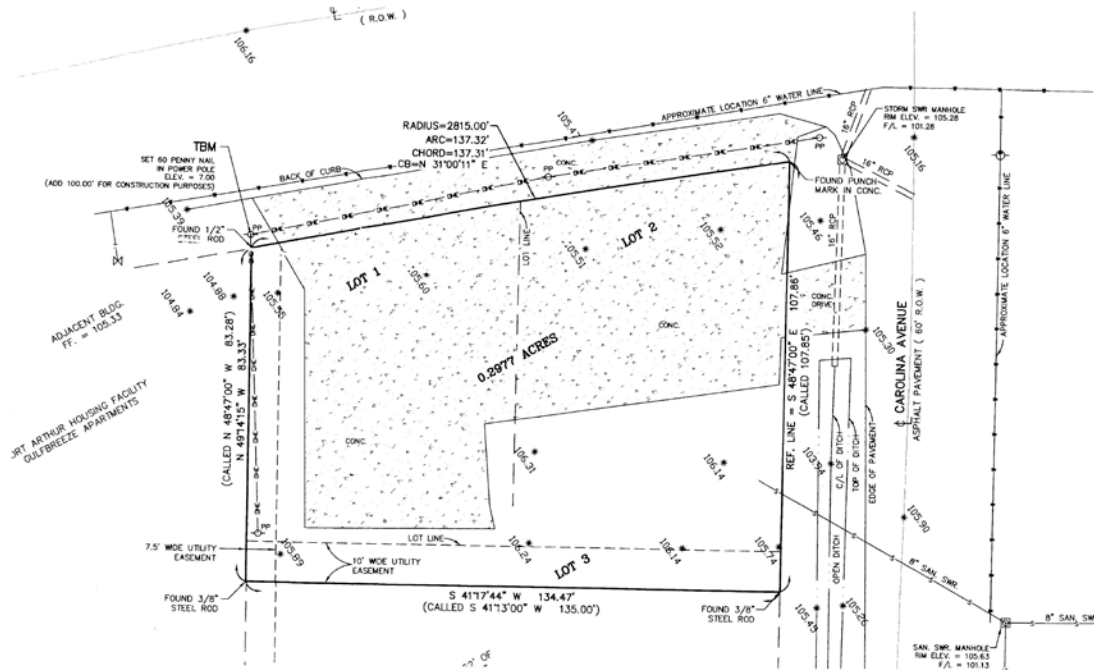
### GULFBREEZE – AS BUILT SURVEY



The Gulfbreeze As Built Survey included in the Authority's records concerning the redevelopment of Gulfbreeze Place. Note that the original legal description and drawing did not include the lots to be used for the learning center, outlined by us in red above. The original development is outlined by us in green, using the metes and bounds in the property description.

## Appendix D

### LEARNING CENTER ORIGINAL SURVEY



The learning center survey provided with the development agreement and building plan to HUD's Office of Public Housing in January 2010. Note that the survey only covered the learning center and did not include the adjacent Gulfbreeze apartments.

## **Appendix E**

### **PROPERTY DESCRIPTIONS**

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Gulfbreeze 1 development, from the Authority's application for disaster recovery funds:

Being a tract or parcel containing 8.980 acres of land out of Lot 7, Block 3, Range F, Port Arthur Land Company Subdivision as recorded in Volume 1, page 22 of the Map of Records of Jefferson County, Texas and also containing 0.099 acre of land being the Southerly 33 feet of Lot 18, Block 40 in Lakeview Third Addition, as recorded in Volume 7, page 92 of the Map of Records of Jefferson County, Texas. It describes the specific metes and bounds of the property.

Vacant tract on which the Authority planned to build the learning center:

A 0.468 acre undeveloped land tract consisting of all of lots 1 and 2 and north 10" of lot 3, block 2, Jones Addition, Jefferson County, Texas.