



Issue Date	March 28, 2011
Audit Report Number	2011-LA-1008

TO: K.J. Brockington, Director, Los Angeles Office of Public Housing , 9DPH  
*Tanya E Schulze*

FROM: Tanya E. Schulze, Regional Inspector General for Audit, Region IX, 9DGA

SUBJECT: The Hawthorne Housing Authority Failed To Maintain an Adequate Financial Management System

## **HIGHLIGHTS**

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

We completed a review of the Hawthorne Housing Authority's (Authority) Section 8 program. We performed the audit based on a recommendation from the Los Angeles U.S. Department of Housing and Urban Development (HUD) Office of Public Housing indicating missing and/or inadequate financial records. In addition, Section 8 reviews are a part of the Office of the Inspector General's (OIG) annual audit plan.

Our objective was to determine whether the Authority used Section 8 Housing Choice Voucher program funds in accordance with HUD rules and regulations. Specifically, we wanted to determine whether the Authority's financial management system was adequate and Section 8 transfers into the City of Hawthorne's (City) general fund were recorded and expended according to HUD rules and regulations.

### **What We Found**

The Authority and City failed to maintain an adequate financial management system to properly administer their Section 8 Housing Choice Voucher program according to HUD rules and regulations. Specifically, the Authority did not properly document more than \$1.4 million in Section 8 investment and interfund activity, making the expended funds

ineligible. Additionally, the Authority accumulated Section 8 deficits due partly to the City's failure to record portability receivables in its accounting system. Lastly, the Authority and City failed to implement adequate internal controls to safeguard and minimize the risk of operating a Section 8 program.

### **What We Recommend**

We recommend that the Director of the Los Angeles Office of Public Housing require the City repay more than \$1.4 million in ineligible expenditures of Section 8 funds and implement adequate policies and procedures over its accounting for interfund activities and portability receivables. In addition, the Director should consider sanctions against the City for not complying with its Annual Contributions Contract.

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

### **Auditee's Response**

We provided the Authority a discussion draft report on February 18, 2011, and held an exit conference with Authority and City officials on March 7, 2011. The Authority provided written comments in two separate responses on March 9 and March 10, 2011, and generally disagreed with our findings.

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

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## **BACKGROUND AND OBJECTIVE**

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The Housing Choice Voucher program was created under the Housing and Urban Rural Recovery Act of 1983 to enable eligible lower income families to obtain modest housing in the private sector that is decent, safe, and sanitary. The U.S. Department of Housing and Urban Development (HUD) provides the rental subsidy to the landlords through public housing agencies.

### **Hawthorne Housing Authority**

The City of Hawthorne (City) operates the Hawthorne Housing Authority (Authority) as part of the City's housing department, located at 4455 West 126<sup>th</sup> Street, Hawthorne, CA. The purpose of the Authority is to administer the Section 8 Housing Choice Voucher program, which provides rental subsidies to very low- and low-income families. The Authority operates its Section 8 program in three segments: administration, regular housing assistance payments, and portable housing assistance payments. It is responsible for tracking, maintaining, safeguarding, and documenting all revenues, expenditures, transfers, and financial details stemming from the use of Section 8 funds. The City's accounting department handles all the fiscal operations of the Authority's Section 8 program, including receivables, payables, deposits, journal entries, tracking fund and cash balances, and fund maintenance. The Authority has a baseline allocation of 711 Section 8 vouchers. As of June 30, 2010, the Authority had 638 vouchers leased and had received more than \$4.9 million for its 2010 housing assistance payments.

### **Portability**

Aside from regular housing assistance, the Authority annually receives a large number of porting vouchers from outside authorities. An eligible family may use a tenant-based voucher to lease a unit anywhere in the United States, leaving the first (initial) public housing agency that issued the voucher for the second (receiving) public housing agency. The receiving public housing agency has the option of administering the subsidy for the initial public housing agency or absorbing the portable family into its own Housing Choice Voucher program. If the receiving public housing agency decides to administer the porting family's subsidy, the housing assistance comes from the initial public housing agency's program allocation. The receiving public housing agency bills the initial public housing agency for the full housing assistance payment and an administrative fee. As of June 30, 2010, the Authority had 518 vouchers leased and had received more than \$4.5 million for its 2010 portable housing assistance payments from outside authorities. On average, the Authority pays monthly housing assistance to other public housing agencies for 20 port-out tenants.

### **Our Objective**

Our objective was to determine whether the Authority used Section 8 Housing Choice Voucher program funds in accordance with HUD rules and regulations. Specifically, we wanted to determine whether the Authority's financial management system was adequate and Section 8

transfers into the City's general fund were recorded and expended according to HUD rules and regulations.

## RESULTS OF AUDIT

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### Finding: The Authority and City Failed To Maintain an Adequate Financial Management System To Properly Track, Maintain, and Expend Section 8 Housing Choice Voucher Program Funds

The Authority and City failed to maintain an adequate financial management system to properly execute their Section 8 program according to HUD rules and regulations. We attribute these deficiencies to the Authority's and City's lack of procedures and controls for the Section 8 program and their disregard for HUD rules and regulations. As a result, the Authority could not provide assurance that more than \$1.2 million in Section 8 investment funds and \$200,000 in Section 8 port Housing Choice Voucher program funds were not used for ineligible costs/activities. Additionally, the Authority could not demonstrate that all port funds were tracked and collected on a timely basis.

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#### **Ineligible Transfer of Section 8 Investment Funds**

The Authority failed to adequately track, record, and document the transfer and expenditure of more than \$1.2 million from a Section 8 investment account. In December 2005, the Authority held more than \$1.2 million in Section 8 investment funds with the State of California's Local Agency Investment Fund. The fund was liquidated in four separate withdrawals and transferred into the City's general fund account. The decision to liquidate and close the Section 8 investment account was made by the former city manager acting as both the city manager and finance director and without notifying the Authority. In addition, there were no approvals or correspondence approving such a large transfer, journal entries recording the transfer ensuring that funds were not comingled, or details of how the funds were expended. The City was only able to provide investment bank statements and master account bank statements showing balances and deposits. After issuance of a subpoena on October 28, 2010, and subpoena compliance letter on December 3, 2010, the City responded on December 30, 2010, certifying that all documents pertaining to our review had been provided to us. Ultimately, the Authority was not able to provide adequate financial records detailing the makeup of more than \$1.2 million in Section 8 funds held in investment and the subsequent transfer and expenditure of the funds into the City's general master account. Therefore, we determined that more than \$1.2 million was ineligible.

Withdrawal date	Withdrawal amount <sup>1</sup>	Ending balance
12/06/05	\$ (1,000,000)	\$ 269,107
10/23/06	(287,558)	-
05/31/07	(889)	-
12/27/07	(8)	-

The Authority disregarded HUD requirements for maintaining adequate financial records to support all Section 8 activity. Although the Authority is responsible for operation and administration of the Section 8 program, the City’s finance department maintains and accounts for the program funds. However, we identified a serious disconnect between the finance and housing departments. The City and Authority utilize different computer data systems that do not collaborate or share information, and the Authority had no other procedures or controls in place to ensure it was aware of how the City was maintaining the program funds and that transactions were properly authorized. The City’s ability to manipulate Section 8 funds without adequate communication and/or approval from the Authority represents a serious lack of internal controls.

**Ineligible Interfund Transfer of Section 8 Portability Funds**

The Authority made an ineligible transfer of \$200,000 in Section 8 portability funds to the City’s general fund. In fiscal year 2007, the Authority borrowed \$650,000 from the City’s general fund, split between Section 8 administration (\$65,000) and Section 8 portables (\$585,000), to cover Section 8 cash deficits. Although the City provided journal entries showing the transfer of funds into the Section 8 administration and portables account, it did not record a payable in the general ledger. In addition, the Authority did not maintain sufficient detail to show what expenditures were covered with the \$650,000 transfer. The Authority repaid \$200,000 of the prior years’ deficits in fiscal year 2008 from the Section 8 portables cash account. As stated in PIH (Office of Public and Indian Housing) Notices 2007-14 and 2008-15, the use of Section 8 funds to cover prior years’ deficits is not allowable. Therefore, we determined that the \$200,000 paid into the general fund account was ineligible. The remaining \$450,000 owed to the general fund would also become ineligible if repaid with Section 8 funds. As above, this occurred due to a general disregard for HUD requirements and a lack of procedures and controls to ensure proper coordination between the Authority and the City’s finance department.

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<sup>1</sup> The differences between amounts withdrawn and prior ending balances were due to accumulated interest deposits.

## **Receivables Not Properly Recorded**

The City did not properly track receivables stemming from the billing and receipt of Section 8 portability vouchers. It did not reconcile whether all Section 8 funds due from HUD and porting entities had been received. While the Authority was responsible for receiving port payments, the City was responsible for entering the payments into the accounting system, including ensuring that receivables were properly recorded when full payment was not received. When funds were not received in full, receivables should have been recorded to balance the general ledger and ensure that fund and cash balances were as accurate as possible; however, these entries were not made.

In a letter, dated December 2005, the former city manager admitted to the City's lack of receivable accounting stating, "Presently we have nothing to indicate which Housing Authority owes us this money (port funds) and thus no means of collecting this sum." The Authority accumulated Section 8 cash deficits in fiscal years 2006 and 2007 and accumulated Section 8 fund deficits in fiscal years 2009 and 2010. We believe the deficits were partly caused by the City's failure to record receivables due from ports and from HUD housing assistance payments. While the Authority had the ability in its HAPPY software to track receivables, this information was not relayed to the City's finance department and was not entered into the City's general ledger accounting system. A lack of communication between the two departments and lack of policies and procedures led to the weakened control environment, allowing poor accounting practices.

## **Conclusion**

We attribute the deficiencies described above to the Authority's and City's disregard for HUD rules and regulations and lack of procedures and controls for the entire Section 8 Housing Choice Voucher program. Overall, we witnessed a poor control environment with a weak management attitude toward ensuring controls were in place and followed. Specifically, the Authority and City failed to maintain an adequate financial management system to properly execute their Section 8 program according to HUD rules and regulations. As a result, the Authority could not provide assurance that more than \$1.2 million in Section 8 investment funds and \$200,000 in Section 8 port Housing Choice Voucher program funds were not used for ineligible costs/activities. Additionally, the Authority could not provide assurance that all port funds were tracked and collected on a timely basis. Ultimately, the lack of procedures and controls put the Authority's Section 8 program at increased risk of waste, fraud, and abuse.



## Recommendations

We recommend that the Director of the Los Angeles Office of Public Housing

- 1A. Require the City to repay the Section 8 program \$1,288,455 for the ineligible expenditure of Section 8 investment funds from non-Federal funds.
- 1B. Require the City to repay the Section 8 program \$200,000 for the ineligible expenditure of Section 8 housing assistance portability funds from non-Federal funds
- 1C. Require the Authority not to repay the remaining \$450,000 transferred from the general fund to the Section 8 program, as the remaining balance would also be considered ineligible if paid back with Section 8 funds.
- 1D. Require the Authority to reconcile portability receivables for fiscal years 2005 through 2011, and seek repayment for outstanding receivables. The outstanding amounts not previously recorded by the Authority would be considered funds to be put to better use.
- 1E. Require the Authority to implement policies procedures to ensure portability receivables are tracked and recorded in coordination with the City's accounting system in accordance with PIH Notice 2008-43.
- 1F. Require the Authority to establish and implement policies and procedures covering the fiscal administration of the Section 8 program.
- 1G. Consider implementing administrative sanctions (i.e., repayment of administrative fees) against the Authority in accordance with 24 CFR 982.152(d) and Section 6 of the Annual Contributions Contract, for failing to comply with its annual contributions contract regarding financial management and maintaining adequate financial records.

## SCOPE AND METHODOLOGY

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We performed our onsite audit work at the Authority, located in Hawthorne, CA, between June and November 2010. Our audit generally covered the period July 1, 2005, through June 30, 2010. We expanded our scope as necessary.

To accomplish our objective, we

- Reviewed applicable HUD regulations, including the Housing Act of 1937, 24 CFR (Code of Federal Regulations) Parts 982, 5, and 985; the Housing Choice Voucher Guidebook 74210.10G; HUD Handbook 7510.1G; and PIH Notices 2007-14, 2008-15, and 2008-43.
- Reviewed the Authority's annual contributions contract, administrative plan, and cost allocation plan.
- Reviewed the City's accounting policies and procedures.
- Interviewed Authority and City management and staff to determine their job responsibilities, Section 8 processes, and control processes and discussed audit-related topics.
- Interviewed the independent auditor responsible for the Authority's annual audits.
- Reviewed records maintained by HUD pertaining to the Authority.
- Reviewed the Authority's financial audit reports for fiscal years 2006, 2007, 2008, and 2009, as well as its staff listing and organizational chart.
- Reviewed Section 8 investment bank statements and City master account bank statements.
- Reviewed detailed accounting records maintained by the Authority and City pertaining to Section 8 interfund transfers, receivables, and Section 8 payments and receipts.

We assessed the reliability of the data provided by the City and Authority. We determined that the Section 8 data provided by the City and Authority is sufficiently reliable, given the audit objectives and intended use of the data. The assessment was conducted on Section 8 investments, interfund transfers, and housing assistance receipts and expenditures. Our assessment included testing journal entries, matching Section 8 expenditures and receipts to general ledger entries, and reconciling bank statements with investment statements. We did note however, the Authority and City do not have adequate policies and procedures for fiscal and program management of the Section 8 program.

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 plans, 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:

- Effectiveness and efficiency of operations – Policies and procedures that the audited entity has implemented to provide reasonable assurance that a program meets its objective, while considering cost effectiveness and efficiency.
- Reliability of financial reporting – Policies and procedures that the audited entity has implemented to reasonably ensure that all financial data, transactions, and reports are accurate and recorded appropriately and in a timely manner.
- Compliance with applicable laws and regulations – Policies and procedures that the audited entity has implemented to reasonably ensure that resource use is consistent with laws and regulations.

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.

## **Significant Deficiency**

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

- The Authority did not have policies and procedures in place to ensure that Section 8 transfers and receivables were tracked, maintained, safeguarded, and expended according to HUD rules and regulations.

## APPENDIXES

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### Appendix A

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

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Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1A	\$1,288,455	
1B	\$200,000	
1C		\$450,000
<b>Total</b>	<b>\$1,488,455</b>	<b>\$450,000</b>

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. These costs consist of Section 8 funds transferred out of the Authority's Section 8 program without adequate tracking, documentation, and safeguarding.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, if the Authority implements our recommendations, it will not repay the City's general fund account with Section 8 funds for a prior interfund transfer, resulting in the Authority's being able to use those funds for other Section 8 needs.

## Appendix B

# AUDITEE COMMENTS AND OIG'S EVALUATION

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### Ref to OIG Evaluation

### Auditee Comments



## City of Hawthorne Housing Department

March 9, 2011

Tanya Schulze  
Regional Inspector General for Audit  
Office of Inspector General  
611 West 6th Street, Suite 1160  
Los Angeles, CA 90017

Dear Ms. Schulze:

I would like to thank you for meeting with us on March 7, 2011. During the meeting I presented to you a copy of our new Portability Policies and Procedures. On February 18, 2011 we received your letter making several recommendations for the Hawthorne Housing Department. In response we have implemented the following new procedures:

1. In reference to recommendation 1D (page 9), we have reconciled the portability receivables for fiscal years 2005 through 2011. We have also sought repayment for outstanding receivables.
2. In reference to recommendation 1E (page 9), we have implemented new Policies and Procedures to ensure portability receivables are tracked and recorded in coordination with the City's accounting system in accordance with PIH Notice 2008-43.
3. In reference to recommendation 1F (page 9), we have established new Policies and Procedures covering the fiscal administration of the Section 8 program.

We would ask you to please not consider implementing any administrative sanctions against the Hawthorne Housing Authority because this would result in our Housing Authority not being able to have enough staff to service our clients and to properly administer the Section 8 Program.

Our finance department will be addressing recommendations 1A, 1B, and 1C. The finance department will be sending you a written response to recommendations 1A, 1B, and 1C.

Thank you once again for your patience with us and for your willingness to work with us. I can be contacted at (310) 349-1603.

Sincerely,

Hamid Pournamdari  
Hawthorne Housing Director

Cc:

**Comment 1**

**Comment 2**

# CITY OF HAWTHORNE



4455 West 126th Street • Hawthorne, California 90250-4482

March 10, 2011

**Via E-Mail, Facsimile & Regular U.S. Mail**

Tanya Schulze  
Regional Inspector General for Audit  
U.S. Department of Housing & Urban Development  
611 West Sixth Street, Suite 1160  
Los Angeles, CA 90017

Dear Ms. Schulze:

This letter responds to draft audit report received from HUD dated February 28, 2011 and date stamped March 3, 2011.

**Response to findings and recommendations:**

**Recommendation 1A Transfer of Section 8 Investment Funds**

The City does not agree with this recommendation.

The audit report assumes that the balance of the City's LAIF account captioned "Housing Authority" consisted of Section 8 investment funds. This assumption is incorrect.

The City's practice during the period covered by the audit was to maintain investment funds on a pooled basis. Consequently the "Housing Authority" LAIF account included pooled funds that did not originate from HUD. Because the funds in the LAIF account did not originate from HUD, it was proper for the City to transfer these funds to the City's general fund.

As evidence that these transfers did not involve HUD funds, we attach a schedule demonstrating that, during each fiscal year from July 1, 2005 through June 30, 2010, the City's expenditures on its Section 8 program *exceeded* the amount of HUD assistance received by the City. Consequently, it is incorrect to assert, as the audit report does, that the City ever possessed \$1,288,455 in HUD investment funds or that transfers from the LAIF account to the City's general fund consisted of HUD investment funds.

We note that the City brought these facts to the Inspector General's Office's attention via an October 26, 2010 letter from Steven Klotzsche, then serving as the City's Interim Finance Director to Tanya Schultze, Regional Inspector General for Audit. To date, the City has not received any response from the Inspector General's Office rebutting the City's explanation of the alleged \$1,288,455 discrepancy.

**Comment 3**



**Comment 4**

The City will ensure that, in the future, HUD funds are not comingled with other City funds.

**Recommendation 1B & 1C Advances made by the City to the Housing Fund of \$200,000 and \$450,000.**

The City does not agree with these recommendations.

As the audit report correctly observes that “in Fiscal Year 2007, the [Housing] Authority borrowed \$650,000 from the City’s general fund.” This advance from the general fund to the housing assistance program was made to ensure that the Authority did not overspend available cash as a result of cash flow issues associated with the Section 8 program. No assertion has been made in the audit report that the Housing Authority spent the advanced \$650,000 on costs that were ineligible under federal Section 8 rules.

The \$650,000 was a loan by the City to the Authority. It was not intended to be a gift or a grant. Indeed, the City has always considered its housing assistance program to be a self-funding program, that neither profits the City’s general fund nor imposes costs upon the City’s general fund. By definition, a loan is made with the intent that the lender will be repaid by the borrower.

To date, as acknowledged by the audit report, the Housing Authority has repaid \$200,000 of the 2007 advance. It is intended that, in the future, the remaining \$450,000 will also be repaid.

The audit report asserts that repayment of the advance is impermissible because “the use of Section 8 funds to cover prior years’ deficits is not allowable.” As support for this assertion, the audit report cites PIH Notices Nos. 2007-14 and 2008-15.

**Comment 5**

We note that the earlier of these two notices was issued on June 18, 2007. According to the City’s records, the last transfer of advanced funds was made from the general fund to the Housing Authority on March 31, 2007. Consequently, the advance was completed *before* HUD notified the City of its policy. The City considers it unreasonable that HUD is trying to retroactively prohibit what the City considers to be a reasonable accounting practice that enabled the effective operation of the City’s housing assistance program for the benefit of housing assistance recipients.

In the future, the City will refrain from making advances from the general fund to the Housing fund unless it is certain that the advance can be repaid during the same fiscal year in which the advance is made.

**Recommendation 1D & 1E Collection of Portability Receivables from Other Public Housing Agencies**

**Comment 1**

The City has established revised procedures to ensure proper collection of Section 8 portability receivables from other public housing agencies. These revised procedures, which the City has provided to HUD staff, are consistent with PIH Notice 2008-43. The City is currently in the process of reconstructing portability collection activity from 2005 to present. The City will ensure that coordination between housing and finance department recordkeeping systems is improved.

**Recommendation 1F Policies and Procedures for Fiscal Administration of Section 8 Program**

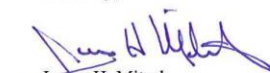
The City is in the process of establishing revised policies and procedures. We plan to have these policies and procedures completed by April 30, 2011.

**Recommendation 1G Administrative Sanctions**

The City requests that no sanctions be imposed. The City has, since the period covered by the audit, hired a new City Manager and a new interim Finance Special Project Manager. The City is in the process of seeking a permanent Administrative Services Director, who will act as Finance Director. The City no longer permits a single person to serve as both City Manager and Finance Director. This new leadership team has cooperated extensively with the HUD Inspector General's Office and is dedicated to ensuring that the City (and its Housing Authority) apply the strictest standards of accountability and transparency. It will strive to ensure that recordkeeping is compliant with all applicable standards and that recordkeeping will be coordinated between the housing and finance departments. We note that there is no evidence that any HUD funding was used by the City for purposes unrelated to the City's housing program. We further note that our outside auditor, Lance, Soll & Lunghard, LLC, has annually audited the City's use of federal funds and never identified any of the issues raised by the audit report. Had our annual outside audits identified the issues, the City would have immediately corrected the issues on a go-forward basis.

**Comment 2**

Sincerely,



James H. Mitsch,  
City Manager  
City of Hawthorne

Cc: Michael Blazenski, Finance Special Project Manager

Additional exhibit made available upon request

## OIG Evaluation of Auditee Comments

**Comment 1** The OIG recognizes the Authority has taken steps to remedy weaknesses identified during our audit. As discussed during the exit conference, the audit resolution process will provide the Authority ample opportunity to present corrective actions for each recommendation to HUD.

**Comment 2** The recommendation for HUD to consider administrative sanctions against the Authority remains unchanged. The recommendation illustrates the significance of the Authority's deficiencies in maintaining a financial management system that tracked, maintained, and safeguarded Section 8 program funds. The control environment did not ensure Section 8 program funds were used according to HUD rules and regulations. As such, we find it appropriate for HUD to consider administrative sanctions.

**Comment 3** We disagree with the City's assessment that the investment account funds were not Section 8 funds. During the audit, the Authority stated the funds held in the investment account consisted of Section 8 reserves accumulated prior to December 2005. The City has never presented any documentation showing the funds held in the Authority's investment account did not originate from Section 8 activities. In December of 2005, the City maintained three separate Local Agency Investment Fund (LAIF) accounts with the State of California, see table below. The City maintained distinct and separate investment funds for the City and redevelopment agency.

Account name	Account number	Ending balance
Hawthorne Housing Authority	25-xx-xxx	\$ 269,107
City of Hawthorne	98-xx-xxx	\$ 6,160,941
Hawthorne Community Redevelopment Agency	65-xx-xxx	\$ 62,546

The City is incorrect in its assertion that we did not respond to the letter from the former interim Finance Director dated October 26, 2010. In a meeting with the former interim Finance Director on November 4, 2010, we discussed the matter and informed the City that it must provide documentation supporting its claims that the Authority's investment fund did not contain any Section 8 funds. We then issued a draft finding outline to the City and Authority on January 20, 2011.

The attachments provided by the City in its response and its earlier response dated October 26, 2010 do not adequately support their claims. The spreadsheets only show cash and fund deficits. The City also stated that during fiscal years from July 1, 2005 through June 30, 2010, the City's expenditures on Section 8 exceeded the amount of HUD assistance. However, The City's financial records showed that in fiscal years ending June 30, 2006 through June 20, 2008, the Authority's Section 8 revenue exceeded the Authority's expenditures for the

program by more than \$2.9 million, which included the period in which the LAIF account funds were liquidated.

In summary, the City was unable to provide any supporting documentation and certified in a subpoena response dated December 30, 2010 that any and all records pertaining to our review have been provided. Therefore, the finding and recommendation remain unchanged and the \$1,288,455 transferred out of the Authority's investment fund account is still considered ineligible.

**Comment 4** We disagree with the City's assertion that the audit report does not question the \$650,000. The report clearly states the Authority was unable to provide supporting documents showing what expenditures the \$650,000 represented. Expenditures merely identified as being applicable to the Section 8 program but without supporting documents are considered ineligible. Again, the City certified in response to our subpoena that all documents were provided. Absent supporting documents, the \$200,000 repaid is considered ineligible and the \$450,000 outstanding would be considered ineligible if repaid.

**Comment 5** We disagree with the City's assessment that the notices cited in the report are not applicable. The initial \$650,000 was transferred to the Section 8 program in four transfers, \$325,000 transferred on December 31, 2006 and \$325,000 transferred on March 31, 2007. While the transfers occurred prior to issuance of PIH Notice 2007-14, the repayment occurred in four installments starting on September 30, 2007, after issuance of the Notice in question. The repayment to the City's general fund used Section 8 funds and therefore violated the provision that Section 8 funds not be used to pay for prior years deficits. Therefore, the finding and recommendation remain unchanged.

Additionally, HUD has placed an increased significance on housing authorities taking steps to ensure their Section 8 programs operate within budget. Public Housing Notice 04-7, section 9, states that the ACC reserve must now cover only those housing assistance payment (HAP) costs that exceed Annual Budget Authority available for HAPs in the current fiscal year. Public Housing Notice 05-1, section 9(C), states authorities must manage their programs in a prudent manner to enable them to serve families within their calendar year 2005 budget and voucher baseline, and that authorities should review their policies and operations to ensure they are not incurring HAP costs beyond what is needed to support decent housing of a modest nature within market rents for participants.

## Appendix C

### CRITERIA

#### **24 CFR 982.158. Program accounts and records.**

- a. The PHA [public housing agency] must maintain complete and accurate accounts and other records for the program in accordance with HUD requirements, in a manner that permits a speedy and effective audit.
- b. The PHA must furnish to HUD accounts and other records, reports, documents and information, as required by HUD.
- c. HUD and the Comptroller General of the United States shall have full and free access to all PHA offices and facilities, and to all accounts and other records of the PHA that are pertinent to administration of the program, including the right to examine or audit the records, and to make copies. The PHA must grant such access to computerized or other electronic records, and to any computers, equipment or facilities containing such records, and shall provide any information or assistance needed to access the records.

#### **24 CFR 982.152(d). Reducing PHA administrative fee.**

HUD may reduce or offset any administrative fee to the PHA, in the amount determined by HUD, if the PHA fails to perform PHA administrative responsibilities correctly or adequately under the program (for example, PHA failure to enforce HQS [housing quality standards] requirements; or to reimburse a receiving PHA promptly under portability procedures).

#### **Annual Contributions Contract (October 23, 1997), Section 6.**

- a. If HUD determines that the HA [housing authority] has failed to comply with any obligations under the consolidated ACC [annual contributions contract], HUD may reduce the amount determined by HUD:
  1. The amount of the HUD payment for any funding increment.
  2. The contract authority or budget authority for any funding increment.
- b. HUD must give HA written notice of the reduction.

#### **Annual Contributions Contract (October 23, 1997), Section 14.**

- a. The Authority must maintain complete and accurate books of account and records for a program. The books and records must be in accordance with HUD requirements, and must permit a speedy and effective audit.
- b. The Authority must furnish HUD such financial and program reports, records, statements, and documents at such times, in such form, and accompanied by such supporting data as required by HUD.
- c. HUD and the Comptroller General of the United States, or their duly authorized representatives, must have full and free access to all HA offices and facilities, and to all the books, documents, and records of the Authority relevant to administration of the program, including the right to audit and to make copies.

**HUD Handbook 7510.1G** states it is the responsibility of the authority to maintain complete and accurate records of all financial management functions. These records must be maintained in a way that will

- Provide an effective system of internal control to safeguard cash and other assets,
- Provide budgetary control over the various programs,
- Provide timely, accurate, and complete financial information for management decision making,
- Provide the authority with financial data needed to prepare required HUD reports, and
- Permit a timely and effective audit.

**HUD Handbook 7510.1G, chapter 2, section 2**, states that the Authority must have records which adequately identify the source and application of funds provided for HUD-assisted activities. These records must contain information pertaining to program awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.

The authority may maintain its own accounting records, or it may contract for accounting services. In either case, it is the responsibility of the authority to maintain financial records which

- Adequately identify the source and application of all program funds and HUD funds,
- Provide the basis for budgetary control and monitoring of financial activities and the financial position of programs,
- Contain the information necessary to determine compliance with budgetary and legal/contractual requirements,
- Provide supporting documentation for transactions and an adequate audit trail, and
- Provide the basis for preparation of required financial reports on a timely basis.

Books and accounts must be complete and accurate. The books of original entry must be kept current at all times, and postings must be made at least monthly to ledger accounts. All records and files must be stored appropriately, and all supporting documentation must be maintained in a safe and accessible location.

**PIH Notice 2007-14.**

Calendar year funds may not be used to cover any prior year deficits. However, PHAs may use funds in the Administrative Fee Equity account for such purposes.

**PIH Notice 2008-15, Section 14(A).**

PHAs may only use CY [calendar year] 2008 HAP [housing assistance payment] funding for housing assistance payments, and only for CY 2008 and future CY HAP needs.

**PIH Notice 2008-15, Section 15.**

CY 2008 funds may not be used to cover any prior year deficits. However, PHAs may use funds in the Administrative Fee Equity account for such purposes.