



U.S. Department of Housing and Urban Development

Office of Inspector General

Region IX

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Audit Memorandum Number

2010-LA-1801

MEMORANDUM FOR: Carolyn O'Neil, Administrator, Southwest Office of Native American Programs, 9EPI

Joan S. Hobbs

FROM: Joan S. Hobbs
Regional Inspector General for Audit, 9DGA

SUBJECT: HUD Should Provide Additional Monitoring of the Navajo Housing Authority's Implementation of Recovery Act-Funded Projects

INTRODUCTION

In accordance with our annual audit plan to review funds provided under the American Recovery and Reinvestment Act of 2009 (Recovery Act), we conducted a capacity review of the Navajo Housing Authority's (Authority) operations. The objective of the review was to evaluate the Authority's capacity to administer its Recovery Act funds and identify related potential internal control weaknesses that could impact its ability to properly administer the funds.

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.

SCOPE AND METHODOLOGY

Our review of the Authority was limited to gaining an understanding of its capacity to administer its Recovery Act funds. To meet our objective, we reviewed Recovery Act documentation and funding agreements. We interviewed Authority management and staff and reviewed Authority documentation such as policies and procedures, organizational charts, and job descriptions. We also interviewed management and staff from HUD's Southwest Office of Native American Programs and reviewed their most recent monitoring report on the Authority. In addition, we reviewed the Authority's recent construction contractor procurement action for its Navajo 45-unit project and construction contractor draw requests for its Apache Trails project. Our review of this

documentation was limited to our stated objective and should not be considered a detailed analysis of the Authority’s internal controls or operations.

We conducted our on-site review from August 4 through August 7, 2009, at the Authority’s Construction Services Division offices in Fort Defiance, AZ.

BACKGROUND

The Recovery Act became Public Law 111-5 on February 17, 2009. The Recovery Act makes supplemental appropriations for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, and State and local fiscal stabilization for the fiscal year ending September 30, 2009, and for other purposes.

The Recovery Act institutes strict obligation and expenditure deadlines with secretarial recapture and reallocation authority. For example, the Authority’s funds must be obligated within 1 year (by May 18, 2010). In addition, at least 50 percent of the funds must be expended within 2 years (by May 18, 2011), and 100 percent must be expended within 3 years (by May 18, 2012). Division A, Title XII, of the Recovery Act provides the appropriations provisions for “Native American Housing Block Grants,” as authorized under Title I of the Native American Housing Assistance and Self-Determination Act of 1996 (NAHASDA). Recovery Act appropriations for Native American programs include \$255 million in funding based upon a formula allocation and \$255 million in funding based upon a competitive allocation. The Authority received \$34.4 million of this funding based upon the formula allocation. This amount represents an increase of 41 percent over the Authority’s fiscal year 2009 NAHASDA grant of \$84.8 million. Authority officials stated that they submitted an application for a \$5 million competitive grant; however, they did not expect to receive this grant.

The Authority’s amended Indian housing plan specifies that its Recovery Act funds will be used as follows:

Program activity	Recovery Act funding amount
Infrastructure and site improvements - repair dilapidated streets in public rental subdivisions	\$ 11,482,620
Energy conservation/efficiency - replace furnaces in public rental units	\$ 8,627,500
Modernization of 1937 Act* units - repair severely damaged public rental units	\$ 3,595,500
Rehabilitation assistance to existing NAHASDA homeowners - repair latent construction defects	\$ 632,654
Bathroom additions - The Authority cancelled this project and had not yet selected a replacement project	\$ 2,106,024
Development - Construct 40 public rental housing units	\$ 7,967,828
Total	\$ 34,412,126

* United States Housing Act of 1937

In an effort to address prior performance problems, including significant audit findings and low housing production levels, the Authority recently decided to change its primary method for construction. Instead of using its force account, the Authority decided to use construction contractors for all construction projects.

RESULTS OF REVIEW

We did not find evidence indicating that the Authority lacked the basic capacity to administer its Recovery Act funding. However, we did identify some concerns that could impact its ability to meet the Recovery Act obligation and expenditure timeframes and ensure that its funds are expended in accordance with program requirements. Additional oversight and technical assistance will be needed to address these issues. Based on our limited review, we noted the following issues:

Policies, Procedures, and Staffing:

- The Authority’s written policies and procedures were originally developed for use by its Grants Management Division, which primarily used subrecipients for construction services. These policies and procedures had not been adapted for use by the Authority’s Construction Services Division, which contracts directly with construction companies. For example, the Authority’s written policies and procedures for development and construction consistently refer to “sub-recipient” roles and responsibilities. The Authority had not reviewed and updated these procedures to specify how these responsibilities would be reassigned or changed to accommodate the Authority’s use of direct contracting within its Construction Services Division.
- Authority officials acknowledged the need for a staffing reorganization within the Authority’s Construction Services Division as they transition from a force account-based construction process to a direct contracting-based process. However, the Authority had not received approval from its board of commissioners to proceed with the proposed reorganization.¹ This condition could impact the Authority’s ability to administer its Recovery Act funding efficiently and effectively because these funds will be expended through direct contracting. For example, the Authority had one procurement specialist, although Authority officials estimated that three would be needed to manage the additional contracting workload under its new direct contracting process.
- The Authority’s record under NAHASDA demonstrated a history of poor management controls, but recent significant staff changes had been made. Our review of the new staff’s qualifications and our observations under this review indicated that management was qualified, experienced, and dedicated to the mission of the Authority.

¹ The auditee’s response indicated that the reorganization was approved by the board of commissioners on October 5, 2009 (see appendix A)

Project Planning:

- In the past, the Authority had problems expending its construction funds in a timely manner. The Recovery Act requires that 50 percent of the funds provided be expended within 2 years of availability and that 100 percent of the funds be expended the following year. A financial status report provided by the Authority showed that it had \$281.3 million in NAHASDA grant funds that were not yet expended for grants from fiscal years 2000 through 2008. The Authority will need to address the expenditure of these funds in addition to the Recovery Act funds totaling \$34.4 million and its NAHASDA formula grant funds for fiscal year 2009 totaling nearly \$84.8 million.
- The Authority's past performance also indicated that it had experienced difficulty in obligating grant funds in a timely manner. This concern was significant because the Recovery Act requires that funds be obligated even more quickly than under existing NAHASDA requirements. Specifically, NAHASDA requires that 90 percent of grant funds be obligated within 2 years, while the Recovery Act requires that 100 percent of the funds be obligated within 1 year. HUD's most recent monitoring report, dated November 2008, noted that the Authority did not meet the NAHASDA 2-year obligation requirement for fiscal years 2002 through 2005, and the report raised concerns regarding whether the Authority would also fail to meet these requirements for fiscal years 2006 and 2007. A financial status report provided by the Authority showed that it had made progress in obligating its grant funds; however, \$88.9 million remained unobligated for grant years 2002 through 2008. The Authority will need to address the obligation of these funds in addition to the Recovery Act funds totaling \$34.4 million and its NAHASDA formula grant funds for fiscal year 2009 totaling nearly \$84.8 million.

Construction project schedules provided by the Authority (updated September 4, 2009) indicated that it would not meet the Recovery Act deadline for obligation of funds for its 40-unit construction project. However, Authority staff members stated that they would revise the schedule for this project to comply with the deadline. Given the Authority's past problems in obligating and expending funds in a timely manner, additional monitoring and technical assistance related to the Authority's implementation of its Recovery Act projects will be necessary to ensure that the Authority proceeds in a timely manner.

- The Authority had not selected a project for \$2.1 million of its Recovery Act funding. Authority officials initially planned to construct 161 bathroom additions for existing homes. However, they realized that they would not be able to meet the Recovery Act funding obligation and expenditure timeframe requirements due to complications associated with obtaining unit eligibility and flood plain determinations. If the Authority does not proceed in a timely manner to identify and plan for an appropriate alternate project, it could have difficulty in meeting the obligation and expenditure deadlines for these funds.

Procurement:

- The Authority was understaffed to handle the preparation and review of bid packages for construction contracts. As noted above, the Authority acknowledged the need to hire additional qualified staff as part of a staffing reorganization plan. However, the reorganization plan had not yet been approved by the Authority's board of commissioners. The need for additional contract specialists will be critical, given that there was only one contract specialist responsible for completing the annual grant funding workload, the backlog of projects from prior grant years, and the additional funding provided by the Recovery Act. This problem could impact the Authority's ability to obligate and expend its Recovery Act funds in a timely manner and in accordance with program requirements.
- The Authority's procurement policies and procedures were not clearly defined or updated. For example,
 - The process for evaluating construction contractors' administrative and financial capacity was not clearly defined. The Authority's written policies and procedures stated that before contracts were awarded, the Authority would ensure that the bidder had the sufficient technical, administrative, and financial capability to perform the contract work of the size and type involved and within the time provided. However, the policies and procedures did not provide specific procedures for how contractor capacity would be established. For example, there were no specific procedures or criteria for verifying and documenting that the contractor had successfully completed previous projects without significant problems. Also there were no specific criteria for determining whether the contractor had the appropriate financial capacity to manage the project successfully.
 - Authority staff indicated that the finance division would be responsible for reviewing the contractors' financial capacity. However, this policy had not been incorporated into the Authority's written policies and procedures.
- We reviewed the Authority's procurement files for its most recently performed construction contractor procurement action (Navajo 45-unit). Based upon this review, we identified the following issues:
 - The procurement file contained no documentation that demonstrated appropriate review of the contractor's financial capacity. The contractor apparently did not submit documentation of its financial resources such as a financial statement and business profiles as required by the Authority's written policies and procedures.
 - The procurement file contained no documentation that demonstrated review of the contractor's administrative capacity and record of past performance. Authority staff members stated that they contacted the owner of the contractor's last project.

However they did not retain documentation of this contact or details regarding the information obtained.

- The procurement file contained no documentation to show that environmental issues noted by the Authority's environmental compliance review officer were addressed. The environmental compliance officer noted concerns with hazardous materials, water management, noise, and air quality and required a report addressing these issues.
- The procurement file did not contain a certification by the contracting officer that the proposed procurement was eligible and that the costs were allowable and reasonable and were consistent with the approved budget as required by the Authority's written policies and procedures. The file also did not contain documentation of the contracting officer's approval of final bid documents.
- The contractor's insurance for the project did not meet the required limits as established by the contract between the Authority and the contractor. Specifically, the employer's liability and general liability insurance had limits that were less than those required by the contract.

Contractor Monitoring and Quality Control:

- Internal controls over construction contractor payment requisitions (draws) were not clearly defined within the Authority's written policies and procedures. These policies were written for use with subrecipients and had not been adapted to the Authority's process of direct contracting. Also, the procedures did not provide specific requirements for documentation and approvals that should be required before the finance department approved the final payment. For example, Authority staff indicated that the inspector's progress reports and the contractor's certified payroll reports would be required as part of the draw documentation. However, the written procedures for draws did not address these items. Also, although the standardized draw forms specified within the written procedures included signature lines for the inspector, contractor, authorized project representative, and contracting officer, the policy did not specifically list all signatures and documentation that were required before final payment was approved. As noted below, the Authority did not consistently apply signature approval requirements in the past. It should be noted that we did not find provisions within the recently executed contract for third-party inspection services requiring the inspector to review and approve the draws.
- The Authority did not implement adequate internal controls to ensure that complete and consistent documentation and approvals were obtained for construction draws. To evaluate the Authority's capacity to consistently apply appropriate documentation and approval standards for draw requests, we reviewed a sample of 16 contractor payment requisitions for a recently completed construction project (Apache Trails). Because Authority officials indicated that their monthly construction meetings held with contractors were used as a control to evaluate the information submitted as part of the draws, we also requested

documentation supporting the performance of these meetings and the associated inspection reports. Based upon this review, we found that

- None of the project draws contained inspection reports or contractor and subcontractor lien waivers. Thirteen of the draws also did not have an associated inspection report as part of the Authority’s monthly meeting documentation.
 - Six of the project draws did not include the Authority’s memorandum form from the “expediter” to the Finance and Accounting Department, which required the Authority’s project manager, labor compliance supervisor, and Construction Services Division director to certify to the value of work in place; that inspections were performed; and that drawings, specifications, and other contract terms were followed.
 - Three of the project draws contained contractor certification forms that were not signed by the Authority’s authorized project representative or contracting officer.
 - Eleven of the draws contained construction progress schedules that were not signed by the project inspector or architect. In two of these cases, there was also no authorization signature from the Authority on the construction progress schedule. In one of these cases, there was also no authorization signature from the Authority or contractor on the construction progress schedule.
 - For nine of the draws, the Authority did not provide documentation supporting the associated monthly construction meeting including the sign-in sheet, agenda, inspection report, and minutes.
 - None of the draw documentation was “notary sealed” as required by the Authority’s policy.
- The Authority did not have internal controls to provide for oversight of its third-party inspection firm to ensure that the inspections were complete, accurate, and in compliance with the terms of the contract.
 - The Authority did not have procedures in place to verify and document correction of deficiencies identified during third-party construction inspections. Further, the Authority did not maintain documentation to support the performance of its own on-site inspections or any associated follow-up to ensure that problems were corrected.

RECOMMENDATIONS

We recommend that the Administrator, Southwest Office of Native American Programs

- 1A. Provide additional monitoring and technical assistance related to the Authority’s implementation of the Recovery Act projects, as needed, to ensure that the Authority has

the appropriate capacity to properly administer its Recovery Act funds. This action should include ensuring that the Authority (1) takes action to proceed with its reorganization or otherwise provide appropriate staffing to manage its new direct contracting-based process and (2) proceeds with its project selection and planning process in a timely manner.

- 1B. Require the Authority to review its written policies and procedures and adapt them to address construction contractor procurement and monitoring. The policies and procedures should include detailed control procedures for processing and approving contractor payment requisitions and reviewing and documenting each contractor's financial and administrative capacity.

AUDITEE'S RESPONSE

We provided a discussion draft memorandum report to the auditee on September 15, 2009, and held an exit conference with its staff on September 29, 2009. The auditee provided written comments on October 7, 2009. It generally agreed with our results.

The complete text of the auditee's response can be found in appendix A of this report. The auditee's response contained a spreadsheet attachment that is not included in Appendix A but is available on request.

Appendix A

AUDITEE COMMENTS

NHA Hooghan—Center of Family Growth, Strength and Beauty **NAVAJO HOUSING AUTHORITY**

October 2, 2009

Joan S. Hobbs, Regional Inspector General for Audit, Region IX
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United States Department of Housing & Urban Development
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RE: OIG ARRA Capacity Review – Draft Report

Dear Ms. Hobbs:

This is in response to your letter dated September 15, 2009 regarding the subject matter. The Navajo Housing Authority (NHA) appreciates the opportunity to provide comments to the draft report issued on NHA's ARRA operations capacity. NHA finds the report to be fair and reflective of operational capacities found at the date of the onsite review. In the respective review categories of the report, the following comments are provided:

Policies, Procedures and Staffing:

NHA acknowledges and agrees with the audit team's review and that the NHA Construction Services Division (CSD) should establish construction policies and procedures to parallel the NHA Grants Management Division's system for the Sub recipient Program. CSD staff is already underway with process mapping of various development and construction activities and actions. NHA expects to complete this effort by December 2009.

Project Planning:

NHA concurs with these observations of past projects that simply lacked project planning and management including quality and payment controls resulting in untimely funds obligations and expenditures. Under a relatively new administration (as of February 2007), NHA is cognizant of this situation and have strived to move the dollars for quicker obligation and expenditure. This backlog of unspent funds is being addressed through recapture and reprogramming of funds from internal NHA projects and Sub recipients that do not have capacity. With respect to current ARRA project schedules, we are enclosing the current correct schedules that coincide with the ARRA timelines.

Procurement:

Again, NHA concurs with the observations noted and a proposed reorganization was initiated by NHA management prior to this review, to address organizational deficiencies

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in contract management expertise. The NHA is pleased to report that the NHA Board of Commissioners (BOC) approved the reorganization on October 5, 2009. As a result, key procurement and construction-related personnel positions will be reclassified and/or created to possess increased skills and knowledge to effectuate proper contract and procurement management functions for a contract-based environment.

Contractor Monitoring and Quality Control

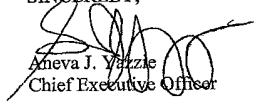
The observation of NHA's internal controls for payments and inspections observations are a subset of the overarching development and construction policies mentioned earlier. NHA acknowledges the need to revamp NHA programs and to establish proper monitoring and quality controls which will also be addressed as part of the process mapping and reorganization rollout of key positions. NHA will accomplish this effort in an expedited manner.

Recommendations:

NHA appreciates the OIG team's recommendation to SWONAP because the technical assistance component was apparently lacking in past years. But under a new administrator, NHA feels confident a unified approach to deliver technical assistance to NHA will greatly benefit our Navajo Nation.

In closing, NHA appreciates the OIG Audit team and its honest review. NHA will take all actions necessary to ensure tightening of our internal control mechanisms and development of policies and procedures for procurement, project and contract management. NHA also looks forward to the technical assistance approach by HUD SWONAP to NHA in order to assure all stringent timelines of the ARRA funding are jointly met and services delivered/jobs created as intended.

SINCERELY,


Aneva J. Yazzie
Chief Executive Officer

Enclosure

XC: Marlene Lynch, CFO
Derrith Watchman-Moore, COO
Paula Puente-Bekis, CAO
Exec Chrono