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Audit Report Number
2011-AT-1008

TO: Maria R. Ortiz, Director of Community Planning and Development, Miami Field Office, 4DD

//signed//

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

SUBJECT: Palm Beach County, FL, Did Not Fully Comply With Federal Requirements When Administering Its Neighborhood Stabilization Programs

HIGHLIGHTS

What We Audited and Why

We audited Palm Beach County, FL's (County) administration of its Neighborhood Stabilization Programs (NSP). We selected the County for review because it received $27.7 million in NSP1 funds, which is more than four times its 2008 Federal fiscal year allocation of Community Development Block Grant (CDBG) funds and the third largest allocation to an entitlement community in the State. In addition, the U.S. Department of Housing and Urban Development (HUD) awarded the County $50 million in NSP2 funds. The audit objective was to determine whether the County's administration of its NSPs complied with Federal requirements. Specifically, we determined whether (1) NSP1 activities met or will meet the low- and moderate-income national objective, (2) program income was properly accounted for, and (3) expended program funds were allowable. In addition, we determined whether expended NSP2 administrative costs were allowable.

What We Found

The County did not fully comply with Federal regulations when administering its NSP1 activities. Specifically, it did not (1) obtain HUD's approval to waive the conflict-of-interest provision, (2) purchase properties at the required purchase discount, and (3) ensure that NSP1 funds expended did not exceed the amounts authorized. In addition, the County did not execute an agreement between its housing department and the facilities department administering the redevelopment activity. The deficiencies resulted in ineligible costs of $1.75 million to the NSP1 program.

In addition, the County did not report accurate program income to HUD. Thus, HUD could not be assured that the County would use an appropriate amount of its program income before drawing down NSP1 funds. As a result, the County had program income of $211,952 that could be put to better use.

The County also did not maintain documentation to sufficiently support the administrative expenditures recorded in its financial system. By not having effective controls, the County could not assure HUD that reviewed administrative expenditures were justified and that accurate program financial results were disclosed. As a result, the County drew down $10,000 in unsupported NSP2 funds.

What We Recommend

We recommend that the Director of the Miami Office of Community Planning and Development require the County to (1) reimburse the NSP1 program $1.75 million from non-Federal funds for ineligible expenditures made from the program, (2) use the $211,952 in program income earned before drawing down additional NSP1 funds, (3) provide supporting documentation or repay the NSP2 program from non-Federal funds for the $10,000 drawn down to reimburse the unsupported workers compensation, and (4) implement policies and procedures to prevent future occurrences of the conditions identified.

For each recommendation in the body of the report 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 the draft audit report to the County for its comments on March 29, 2011. On April 8, 2011, we met with County officials to discuss the report and obtained its written response. In its response, the County generally agreed with the three findings and recommendations, but requested reconsideration on two loans under the conflict-of-interest issue. The complete text of the County's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVE

On July 30, 2008, Title III of Division B of the Housing and Economic Recovery Act of 2008 (HERA) authorized $3.92 billion for the redevelopment of abandoned and foreclosed-upon homes and residential properties. The U.S. Department of Housing and Urban Development (HUD) established the grant amounts to the States and units of general local government based on a funding formula. The funds are treated as Community Development Block Grant (CDBG) funds. This grant program, referred to as the Neighborhood Stabilization Program (NSP), provides targeted emergency assistance to State and local governments to acquire and redevelop foreclosed-upon properties that might otherwise become sources of abandonment and blight within their communities. NSP1 references the grant program authorized under HERA.

On February 17, 2009, Title XII of Division A of the American Recovery and Reinvestment Act of 2009 (Recovery Act) authorized additional funding for the provision of emergency assistance for the redevelopment of abandoned and foreclosed-upon homes as authorized under HERA. Funds of $1.93 billion were awarded through competition. Eligible applicants included States, units of general local government, nonprofits, and consortia of nonprofits. NSP2 references the grant program authorized under the Recovery Act.

On March 9, 2009, HUD granted Palm Beach County, FL (County), $27.7 million in NSP1 funds, and on February 11, 2010, HUD awarded the County $50 million in NSP2 funds. The County's Department of Housing and Community Development (housing department) is the lead department for both programs. The housing department administers Federal-, State-, and County-funded programs. This responsibility includes administering programs that provide affordable housing, a better living environment, and economic opportunities for county residents, emphasizing lower income residents, the homeless, and special needs populations.

For NSP1, the County uses the funds to administer three activities and for administration and planning. As of December 31, 2010, 60 percent of the funds had been expended.

#	Project/activity title	Description	NSP1 funds budgeted	NSP1 funds expended
1	Financing mechanism	The provision of first and second mortgages to income-eligible home buyers to acquire and rehabilitate foreclosed-upon single-family homes.	$12,845,811	$ 8,873,396
2	Redevelopment of vacant land	The acquisition and rehabilitation of a facility to be redeveloped as a homeless resource center.	$ 7,500,000	$ 3,035,333
3	Purchase & rehabilitation	The acquisition and rehabilitation of vacant, abandoned, and foreclosed-upon residential properties by subrecipients to be resold or rented to eligible home buyers or tenants.	$ 5,000,000	$ 3,494,937
4	Administration and planning		$ 2,354,529	$ 1,281,924
	Total		**$27,700,340**	**$16,685,590**

For NSP2, the County uses the funds to administer three activities to stabilize a 25-square-mile area of unincorporated central Palm Beach County and for administration and planning. As of January 10, 2011, about 1 percent of the funds had been expended.

#	Project/activity title	Description	NSP2 funds budgeted	NSP2 funds expended
1	Financing mechanism	The provision of forgivable second mortgages to income-eligible home buyers to subsidize the acquisition of foreclosed-upon single-family housing units for owner occupancy.	$ 9,150,000	$-
2	Residential Redevelopment Program	The provision of grant funds to subrecipients to purchase and rehabilitate abandoned, vacant, or foreclosed-upon residential properties to be resold, rented, or redeveloped to provide affordable housing. The revenues generated will be considered program income.	$20,130,000	$-
3	Neighborhood Redevelopment Program	The provision of loan funds to subrecipients to redevelop demolished or vacant properties as affordable rental housing. The revenues generated will not be considered program income.	$16,470,000	$-
4	Administration and planning		$ 4,250,000	$328,404
	Total		**$50,000,000**	**$328,404**

As of January 2011, the County had requested approval from HUD to change the scope of the financing mechanism activity to also provide first mortgages to eligible home buyers. HUD had not agreed to the change, and the County was waiting for technical assistance to move forward with the activity. For the residential and neighborhood rental redevelopment programs, the County had received requests for proposals from interested entities and was making its selection.

The audit objective was to determine whether the County's administration of its NSPs complied with Federal requirements. Specifically, we determined whether (1) NSP1 activities met or will meet the low- and moderate-income national objective, (2) program income was properly accounted for, and (3) expended program funds were allowable. In addition, we determined whether expended NSP2 administrative costs were allowable.

RESULTS OF AUDIT

Finding 1: The County Did Not Fully Comply With Regulations When Administering NSP1 Activities

The County did not fully comply with Federal regulations when administering its financing mechanism and redevelopment of vacant land activities. Specifically, it did not (1) obtain HUD's approval to waive the conflict-of-interest provision, (2) purchase properties at the required purchase discount, and (3) ensure that NSP1 funds expended did not exceed the amounts authorized. In addition, the County did not execute an agreement between the housing department and the department administering the redevelopment activity. These conditions occurred because the County did not have adequate controls to ensure its compliance with Federal regulations. The deficiencies resulted in ineligible costs of $1.75 million to the NSP1 program.

The Financing Activity Did Not Comply With Requirements

The County used NSP1 funds to provide first and second mortgages to eligible home buyers. The first mortgage loan amount was determined by the home buyer's financial condition and was payable to the County in monthly mortgage payments. The second mortgage grant amount was determined by the home buyer's income status and did not have to be repaid unless the property was sold or transferred within 30 years. A home buyer who was very low income qualified for up to $100,000 in subsidy, a low-income home buyer qualified for up to $75,000, and a moderate-income home buyer qualified for up to $25,000. The two mortgages assisted the home buyer with the purchase of the property, closing costs, and repair costs. As of November 8, 2010, the County had provided mortgages to 68 home buyers. We reviewed 26 of the 68 loan files and found that the County did not fully comply with Federal requirements when administering the activity. See appendix C for a list of the 18 loans reviewed with deficiencies and the ineligible costs associated with each loan.

Conflict of Interest

The County did not obtain HUD's approval to waive the conflict-of-interest provision in 24 CFR (Code of Federal Regulations) 570.611(b) and (c) before providing mortgages to nine County employees and the daughter of one County employee who worked in the housing department. HUD regulations state that no persons defined as a covered person, who exercise or have exercised any functions or responsibilities or are in a position to gain inside information with respect to CDBG activities, may obtain a financial interest or benefit from a CDBG-assisted activity for themselves or those with whom they have business or immediate family ties, during their tenure or for 1 year thereafter. A covered person is defined as a person who is an employee, agent, consultant, officer, or elected or appointed official of the grantee, designated public agencies, or subrecipients. Further, 24 CFR 570.611(d) states that upon the grantee's written request, HUD may grant an exception to the provision on a case-by-case basis when it has satisfactorily met the threshold requirements.

For six home buyers, documentation in the loan files showed that the County obtained the Board of County Commissioners' approval before providing them with mortgages. However, the files did not contain evidence that the County received HUD's approval to waive the conflict-of-interest provision for all 10 home buyers. The County stated that it did not know it had to obtain approval from HUD. By not advising HUD and obtaining its approval, the County could not assure HUD that the home buyers who were provided NSP1 funding did not possess a conflict of interest. Therefore, in the absence of HUD's waiver, the mortgages for the 10 home buyers, totaling $1.7 million, were ineligible costs to the program.

Purchase Discount

HERA, Section 2301(d)(1), states that any purchase of a foreclosed-upon home or residential property shall be at a discount from the current market appraised value, taking into account its current condition, and such discount shall ensure that purchasers are paying below market value for the property. The June 19, 2009, Federal Register, 74 FR 29225 requires the discount to be at least 1 percent from the current market appraised value.

The County did not purchase seven properties at a 1 percent discount from the current market appraised value as required by Federal regulations. The County explained that it had previously applied the 1 percent discount to the property's appraised value subject to repairs. In April 2010, it changed the policy to apply the discount to the current market appraised value. However, the County reasoned that its previous policy of applying the 1 percent discount on the subject-to-repair value was not an incorrect interpretation of the regulations, with the rationale that the property's value was not changed by bringing the property up to code or making it habitable.

As stated by the Federal requirements, the 1 percent discount should be applied to the property's current market appraised value, considering its current condition. By not purchasing a property at a discount, the home buyer and/or the County unnecessarily paid more for the property. Therefore, the excess amount paid on the seven properties was an ineligible cost to the program. We did not question the excess costs paid for three properties. For one property, the County transferred the expenditures related to the property out of the NSP1 fund and used another funding source to pay for them. For the other two properties, the excess costs were not questioned because the home buyers were County employees and their mortgages were questioned under the conflict-of-interest issue above.

Consequently, the excess amount paid of $24,090 for the remaining four home buyers was an ineligible cost to the program.

Excess Disbursed Funds

The County did not ensure that the NSP1 funds disbursed for four home buyers did not exceed the amount authorized by the mortgage agreements. The excess disbursements occurred when the County approved and disbursed additional repair costs without also increasing the home buyer's mortgage amount. For example, in one loan, the County authorized $140,730 in first and second mortgages to the home buyer but disbursed $8,836 more than the authorized amount for the additional repair costs. HUD regulations at 24 CFR 85.20(b) state that the grantee must maintain effective control and accountability for all grant cash, real and personal property, and other assets. In addition, grantees must maintain accounting records that adequately identify the source and application of funds provided.

The County was unaware of the issue. It remedied three of the four loans once the issue was disclosed during our review. For one loan, the County used State funds to repay the NSP1 program, thereby paying the $4,170 excess amount with the State funds. For another loan, it increased the amount on the home buyer's first mortgage to cover the $850 excess amount. The home buyer's financial condition supported the increase to the mortgage. For the third loan, the County increased the amount on the home buyer's second mortgage to cover the $2,825 excess amount. Since the County qualified the home buyer as low-income and it allowed low-income home buyers to receive up to $75,000 in second mortgage subsidies, the County was able to increase the home buyer's second mortgage amount from $58,500 to $61,325.

The excess disbursements occurred because the County did not have a process in place to ensure that the disbursements expended on behalf of the home buyer did not exceed the authorized mortgage amount for the home buyer. By not maintaining effective controls, the County disbursed more for the home buyer than it encumbered for the home buyer. For the remaining loan, the excess amount disbursed of $8,836 was an ineligible cost to the program.

The Redevelopment Activity Did Not Have an Agreement

The County used NSP1 funds to acquire and rehabilitate a facility to be redeveloped as a homeless resource center. Our review indicated that the County's Facilities Development and Operations Department (facilities department) had primary responsibility for this project in that it had the authority to make decisions that affected the outcome of the project and to authorize payments to the contractors. The housing department had no direct oversight. It reported the activity's progress to HUD and reimbursed the facilities department after it made the payments.

HUD regulations at 24 CFR 570.501(b) state that when a unit of general local government is participating with or as part of an urban county or as part of a metropolitan city, the recipient is responsible for applying to the unit of general local government the same requirements as are applicable to subrecipients. Chapter 1-7 of Managing CDBG: A Guidebook for Grantees on Subrecipient Oversight further clarifies that because 24 CFR 570.501(a) provides that local governments are subject to the same requirements as subrecipients, interagency or interdepartmental agreements should include the same provisions as those required in a subrecipient agreement that is described in 24 CFR 570.503(b).

The County did not execute an agreement between the housing department and the facilities department. Housing department officials did not believe that an agreement between the two departments was necessary and confirmed that no agreement existed between the departments that complied with 24 CFR 570.503(b). By not having a written agreement to delineate the responsibilities of each department, the housing department, as the designated department, may not have had adequate control over or accountability for the decisions made by the facilities department, which may negatively impact the project's program objective.

Conclusion

The County did not fully comply with Federal regulations when administering its financing mechanism and redevelopment of vacant land activities. For the financing mechanism activity, the County did not (1) obtain approval from HUD to waive the conflict-of-interest provision in HUD requirements, thereby not assuring HUD that the home buyers did not have a conflict of interest; (2) purchase properties at the required 1 percent discount, thereby unnecessarily paying more for the property; and (3) ensure that funds disbursed for the home buyer did not exceed the amount authorized for the home buyer, resulting in the disbursements recorded in the County's financial system being more than the amounts obligated for the home buyer. For the redevelopment of vacant land activity, the County did not execute an agreement between the lead department and the administering department, which may have resulted in the housing department's not having adequate control over or accountability for the activity. The County did not have adequate controls in place to ensure its compliance with Federal regulations. The deficiencies resulted in ineligible costs of $1.75 million to the NSP1 program.

Although this finding relates to the NSP1 program, the County also uses NSP2 funds to provide mortgages to eligible home buyers. Thus, the County needs to implement controls to prevent the deficiencies identified in the NSP1 financing mechanism activity from occurring in its NSP2 program.

Recommendations

We recommend that the Director of the Miami Office of Community Planning and Development require the County to

1A. Reimburse the NSP1 program $1,719,021 from non-Federal funds for the mortgages provided to the nine County employees and one home buyer related to the housing department employee.

1B. Reimburse the NSP1 program $24,090 from non-Federal funds for the excess amount paid on four properties that were not purchased at the required 1 percent discount of the current market appraised value.

1C. Implement corrective measures to remedy the one loan in which the disbursed NSP1 funds for the home buyer exceeded the authorized mortgage amount or reimburse the NSP1 program $8,836 from non-Federal funds for the excess amount.

1D. Develop and implement policies and procedures for its NSP programs to ensure that it will (a) obtain HUD’s waiver before approving mortgages for County employees, (b) purchase foreclosed-upon properties for at least a 1 percent discount from the current market appraised value, and (c) not disburse funds in excess of the authorized mortgage amount.

1E. Execute an agreement, which complies with 24 CFR 570.503(b), between the housing department and the facilities department for the activity to redevelop the vacant land into a homeless resource center.

Finding 2: The County Did Not Report Accurate NSP1 Program Income to HUD

The County did not report accurate program income in HUD's Disaster Recovery Grant Reporting system (system) as required by Federal regulations. This condition occurred because the County had inadequate controls to ensure that it reported accurate and timely program income. By not reporting accurate and timely program income to the HUD system, the County could not assure HUD that it would use an appropriate amount of its program income before using additional NSP1 funds. As a result, the County had program income of $211,952 that could be put to better use.

Accurate Program Income Was Not Reported to HUD

HUD regulations at 24 CFR 570.500 define program income as gross income received by the grantee directly generated from the use of program funds. Regulations at 24 CFR 570.504(a) require that the receipt and expenditure of program income be recorded as part of the financial transactions of the grant program. The October 6, 2008, Federal Register, FR-5255-N-01, Section II.O1.b., requires that each grantee report its NSP funds to HUD using the HUD system and submit a quarterly performance report. Section II.N3. of the same Federal Register further states that all program income must be disbursed for eligible NSP activities before additional cash withdrawals are made.

The County's NSP1 activities have generated and will continue to generate program income. For the redevelopment activity, the County earned program income when tenants made lease payments for the few months they stayed before moving out of the acquired facility. For the financing mechanism activity, the County earned program income when the home buyer paid the principal and interest payments on the mortgage. In addition, for the purchase and rehabilitation activity, the County will earn program income when the subrecipient resells the property it acquired and rehabilitated and can earn program income when the subrecipient rents the property and the rental income exceeds the operating expenses of the property.

The County had earned and recorded in its financial system $211,952 in program income as of December 31, 2010. However, it reported only $73,319 in program income in the HUD system. This discrepancy resulted in a $138,633 difference in program income that was not reported to the system. The table below lists the amount of program income recorded in the County's financial system and reported to the HUD system for the past four quarters.

Quarter	County financial system	HUD system	Difference*
January-March 2010	$ 22,622	$ 0	$ 22,622
April-June 2010	$ 44,565	$ 61,999	($ 17,435)
July-September 2010	$ 66,715	$ 5,187	$ 61,527
October-December 2010	$ 78,051	$ 6,132	$ 71,919
Total*	**$211,952**	**$ 73,319**	**$138,633**
* Difference due to rounding.			

The County did not report accurate and timely program income in the HUD system as required by Federal regulations. It did not have adequate controls in place to ensure that program income was reported accurately and in a timely manner to the HUD system. A housing department official, who was responsible for reporting program income to the system, stated that he was not sure how to report the program income information to the system and was not sure he had access to do so. By not reporting accurate and timely program income to the HUD system, the County could not assure HUD that it would use an appropriate program income amount before drawing down additional NSP1 funds. The County did not use the program income before drawing down additional funds. The HUD system indicated that although the County drew down program funds in the October 1 to December 31, 2010, quarter, it did not use any of its earned program income. Thus, the program income of $211,952 that the County earned up to December 31, 2010, would be funds to be put to better use.

Conclusion

The County did not report accurate and timely program income in the HUD system and did not use its earned program income before drawing down additional NSP1 funds. By not having adequate controls, it had program income of $211,952 that could be put to better use.

Although this finding relates to the NSP1 program, the County uses funds for NSP2 activities that will generate program income. Thus, it needs to implement controls to ensure that accurate program income will be reported in the HUD system and will be used before drawing down NSP2 funds.

Recommendations

We recommend that the Director of the Miami Office of Community Planning and Development require the County to

2A. Use the $211,952 in program income earned before drawing down additional NSP1 funds.

2B. Develop and implement policies and procedures to ensure that it will report accurate program income information in the HUD system and use the program income before drawing down additional NSP funds.

Finding 3: The County Did Not Sufficiently Support NSP2 Administrative Expenditures

The County did not maintain documentation to sufficiently support the administrative expenditures recorded in the County’s financial system. Specifically, it did not have documentation to support workers compensation and indirect cost and did not ensure that documentation supported the salary and benefit charges. This condition occurred because the County did not have adequate controls to ensure that it maintained sufficient documentation to support program expenditures and reported accurate program expenditures. By not having effective controls, the County could not assure HUD that reviewed administrative expenditures were justified and that accurate program financial results were disclosed. In addition, the County drew down $10,000 in NSP2 funds for unsupported workers compensation costs.

Given the program’s limited progress, the County had expended funds for only administrative costs. We reviewed administrative costs in the areas of workers compensation, indirect cost, and salaries and benefits due to their relative high dollar amounts.

The County did not maintain documentation to sufficiently support the reviewed expenditures recorded in the County’s financial system. HUD regulations at 24 CFR 85.20(b) state that the grantee must maintain records which adequately identify the source and application of funds provided and these accounting records must be supported by source documentation. Further, the grantee must maintain effective control and accountability for all grant and subgrant cash, real and personal property, and other assets.

Administrative Expenditures Were Not Supported

<u>Workers Compensation</u>
The County charged $10,000 in workers compensation to the NSP2 program. County officials stated that they did not know why the $10,000 was charged to the program and had no documentation to support the charge. The $10,000 had been drawn down and reimbursed by NSP2 funds. Therefore, since the amount was not sufficiently supported, the $10,000 was an unsupported cost to the program.

<u>Indirect Costs</u>
The County charged $75,000 in indirect cost to the NSP2 program. County officials stated that they did not know how the $75,000 amount was determined and did not have the documentation to support the amount. After our inquiry, the County reversed the $75,000 charge to the NSP2 program. The expenditure had not been used to support a drawdown.

Salaries and Benefits Were Not Accurately Recorded

The County did not accurately charge salaries and benefits to the NSP2 program. Unless an employee whose salary and benefits are charged to the NSP2 program works his/her full hours on the program, 100 percent of his/her salary and benefits will not be charged to the program. When the employee works on both the NSP2 and other programs, the applicable percentage of the employee's salary and benefits is charged to the program on which he/she worked based on timesheets. The County made the adjustments to the salaries and benefits at the end of the quarter.

For the July to September 2010 quarter, the County did not accurately distribute an employee's salary and benefits among the programs on which the employee worked because it erroneously calculated them using the wrong percentages. Although the timesheet showed that the employee worked 60 percent on NSP2 and 40 percent on other programs, the County charged 60 percent of the salary and benefits to the other programs. In addition, the County did not charge another employee's salary and benefits to the applicable programs on which the employee worked because it had not obtained the employee's timesheet when it made the salary and benefit adjustments for the quarter. Our review of the salary and benefit information prompted the County to correct the salary and benefit amounts reported in the financial system. It provided journal vouchers to show that adjustments were made to the NSP2 program for the quarter.

For the October to December 2010 quarter, the County did not accurately distribute an employee's salary and benefits among the programs worked on because the employee had not submitted the timesheets when the County made the adjustment. By not having the employee's timesheets to appropriately distribute the salary and benefits among the programs worked on, the County recorded inaccurate information in the financial system, which may have resulted in inaccurate drawdown amounts of NSP2 funds.

Conclusion

The County did not maintain documentation to sufficiently support the administrative expenditures recorded in its financial system. Specifically, it did not have documentation to support workers compensation and indirect cost and did not ensure that documentation supported the salary and benefit charges. The conditions occurred because the County did not have adequate controls in place to ensure that it maintained sufficient documentation to support NSP2 administrative expenditures and reported accurate NSP2 administrative expenditures. By not maintaining documentation to support the workers compensation and indirect cost, the County could not assure HUD that these expenditures were justified. In addition, the County's financial system did not disclose accurate financial results of the NSP2 program. This condition also resulted in a $10,000 drawdown of unsupported NSP2 funds.

Although our review of the NSP2 program was limited to the administrative costs, the deficiencies identified with the County's administration of the NSP1 program may affect its administration of its NSP2 program if adequate controls are not implemented to prevent such deficiencies. For example, the County uses both NSP1 and NSP2 funds to provide mortgages to eligible home buyers. Thus, it needs to ensure that HUD approval is obtained before NSP funds are awarded to a County employee or that a foreclosed-upon property is purchased at a 1 percent discount from the current market appraised value (refer to finding 1). In addition, both NSP1 and NSP2 activities will generate program income. Thus, the County needs to ensure that accurate program income is reported in HUD's system (refer to finding 2).

Recommendations

We recommend that the Director of the Miami Office of Community Planning and Development require the County to

3A. Provide documentation to support the $10,000 used to pay for workers compensation or reimburse the NSP2 program from non-Federal funds.

3B. Provide documentation to support the fiscal year 2011 indirect cost expenditure before it draws down NSP2 funds for reimbursement.

3C. Determine the salary and benefit amounts for the applicable programs worked on by the employees and take corrective measures to report the accurate salary and benefit amounts for the period.

3D. Develop and implement policies and procedures to ensure that (1) sufficient documentation is maintained to support budgeted cost items like indirect costs and workers compensation and (2) accurate salary and benefit amounts are charged to the NSP2 program.

SCOPE AND METHODOLOGY

Our objective was to determine whether the County complied with Federal requirements when administering its NSPs.

To accomplish our objective, we

- Reviewed relevant Federal regulations and HUD handbooks;
- Reviewed the County's applications for the NSP1 and NSP2 grants, the County's and housing department's organizational structure, published audit reports from the County's Internal Audit Office, and published single audit reports;
- Interviewed HUD officials to clarify HUD requirements and discuss findings;
- Interviewed County officials to understand the policies and procedures staff follow to carry out the NSP1 activities and to obtain clarifications during the fieldwork;
- Reviewed the County's programmatic and fiscal files related to the NSP1 financing mechanism, redevelopment of vacant land, and purchase and rehabilitation activities;
- Analyzed the expenditure and revenue reports from the County's financial system; and
- Analyzed the journal vouchers used to charge off an employee's salary and benefits to and from the NSP2 program.

For the financing mechanism activity, the County provided a spreadsheet listing the 68 home buyers who closed as of November 8, 2010, with mortgages totaling more than $9.98 million. During the audit, we reviewed 26 of the 68 closed loans, totaling about $4 million, or 40 percent of the total mortgages. We selected the loans based on (1) the large dollar amount of NSP funds disbursed for the home buyer, (2) home buyers identified as County employees, (3) comparing the appraised value of the property listed on the County-provided spreadsheet with the sales price recorded on the County's property appraiser Web site, and (4) comparing the NSP1 amount funded to the home buyer as listed on the County-provided spreadsheet with the disbursement for the home buyer as recorded in the County's financial system.

For the redevelopment of vacant land activity, we reviewed the activity as a whole and also reviewed the more than $2.7 million it had disbursed as of September 30, 2010. For the purchase and rehabilitation activity, we selected 10 of the 25 properties acquired by the 8 subrecipients for review; 1 property each from 6 subrecipients, and 2 properties each from 2 subrecipients. The acquisition cost of the selected properties total $1.3 million, or 45 percent of the $2.9 million expended on the properties as of November 19, 2010. Generally, the properties were selected based on the high dollar amount of their acquisition cost. We did not perform a 100 percent review of the loans/properties for the financing mechanism or purchase and rehabilitation activities. The results of the audit apply only to the items reviewed and were not projected to the universe of loans/properties.

In addition, we determined whether the County maintained sufficient documentation to evidence that program income was properly accounted for by assessing whether (1) the activity generated program income; (2) the income was remitted to the County and if so, how much and when; (3) the income was recorded in the County's financial system, and (4) the income was reported to HUD's system.

We also obtained a status of the County's NSP2 program. Given the program's limited progress, the County only expended funds for administrative costs. As of January 10, 2011, the County had expended $328,404 in administrative costs. We selected the administrative expenditures of salaries and benefits, indirect cost, and workers compensation due to their relative high dollar amounts. The selected expenditures totaled $129,273 or 39 percent of the expended administrative costs.

We tested the reliability of the computer-processed data reported in the County's financial system as they related to our audit objective. Specifically, we assessed whether the expenditure and revenue amounts were accurate and complete. We compared and reviewed the source documents in the loan files and fiscal files to assess the reliability of the expenditures and revenues reported in the County's financial system. We found that the expenditures and revenues reported in the County's financial system were sufficiently supported, and, thus, were accurate and could be relied upon for our audit purposes.

Our review generally covered the period October 1, 2008, to September 30, 2010, and was extended as needed. The work was performed from October 2010 to March 2011 at the housing department located at 100 Australian Avenue, Suite 500, West Palm Beach, FL, and our Miami office.

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

INTERNAL CONTROLS

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.

Relevant Internal Controls

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

- Controls over program operations;
- Controls over the reliability of data;
- Controls over compliance with laws and regulations; and
- Controls over the safeguarding of resources against waste, loss, and misuse.

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 Deficiencies

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

- The County did not fully comply with Federal regulations when administering two NSP1 activities (finding 1).
- The County did not report accurate program income to the HUD system (finding 2).
- The County did not sufficiently support NSP2 administrative expenditures (finding 3).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Unsupported 2/	Funds to be put to better use 3/
1A	$1,719,021		
1B	$24,090		
1C	$8,836		
2A			$211,952
3A		$10,000	
Total	$1,751,947	$10,000	$211,952

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.

2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

3/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (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 County implements recommendation 2A, funds will be used for other eligible activities consistent with HUD requirements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Refer to OIG Evaluation **Auditee Comments**

PALM BEACH COUNTY FLORIDA

Housing and Community Development

Planning

100 Australian Avenue - Suite #500

West Palm Beach, FL 33406

(561) 233-3600

FAX: (561) 233-3651

www.pbcgov.com/hcd

Palm Beach County Board of County Commissioners

Karen T. Marcus, Chair

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Paulette Burdick

Steven L. Abrams

Burt Aaronson

Jess R. Santamaria

Priscilla A. Taylor

County Administrator

Robert Weisman, P.E.

"An Equal Opportunity Affirmative Action Employer"

April 8, 2011

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

Dear Mr. McKay:

Palm Beach County is in receipt of the discussion draft audit report on your review of the Neighborhood Stabilization Program which was recently prepared by your staff. As recommended in the cover letter which transmitted this report to HCD, Palm Beach County hereby submits its comments on the draft report for inclusion in the final report.

FINDING 1- THE COUNTY DID NOT FULLY COMPLY WITH REGULATIONS WHEN ADMINISTERING THE NSP1 ACTIVITIES.

The Financial Activity Did Not Comply With Requirements

Comment 1

***Conflict of Interest*- HUD's permission was not obtained to waive the Conflict of Interest Provision before providing mortgages to nine employees and to the daughter of one employee.**

HUD's Recommendation- The County is to reimburse the NSP1 Program $1,719,021 from non-Federal funds.

County Response Palm Beach County is in agreement with this finding as it relates to eight of the ten cases cited and will agree to refund the NSP1 program account the $1,335,310.00 associated with those cases. The eight cases and the associated amounts to be repaid are detailed on the table below. These files will be transferred to another non-Federal repayable first mortgage program. We are seeking a reconsideration of the IG determination on the remaining two cases, (loan #1-0600-00920101 and loan # 1-0600-0112509). In the case of loan number 1-0600-00920101, the borrower is an employee of the Clerk and Comptroller, and not of the Board of County Commissioners. In the case of loan number 1-0600-01125091, at the time of application and funding approval, the co-applicant was not an employee of the Board of County Commissioners. After becoming an employee of the Board of County Commissioners, the applicant divorced on February 10, 2010. The divorced co-applicant no longer resides in the NSP

Comment 2

assisted property. Furthermore, the Palm Beach County Attorney's office is in the process of making a recommendation for the co-applicant to sign a Quit Claim Deed which would provide sole ownership to the party who is not a Board of County Commissioners employee. The County will reimburse the $1,335,310.00 associated with the other cases on August 1, 2011.

#	Loan #	NSP1 Funds
Cases to be Refunded by Palm Beach County		
1.	1-0600-00129101	$212,800.00
2.	1-0600-00630102	$208,000.00
3.	1-0600-00630101	$189,000.00
4.	1-0600-01029101	$150,000.00
5.	1-0600-00409101	$184,090.00
6.	1-0600-00520101	$163,400.00
7.	1-0600-01214091	$117,713.00
8.	1-0600-01210091	$100,307.00
	Total to be Reimbursed	**$1,335,310.00**
Cases for which relief is being sought		
1.	1-0600-01125091	$196,098.00
2.	1-0600-00920101	$197,613.00
	Total relief being sought	**$393,711.00**

Purchase Discount **- Seven properties were not purchased at a 1% discount below the appraised market value. The fiscal impact of this finding only relates to four of the seven properties since: for one property the excess costs related to its acquisition was transferred to another funding source; and for the remaining two, these were already questioned under the conflict of interest finding above.**

HUD's Recommendation- The County should reimburse the NSP1 Program $24,090 from non-Federal funds.

County Response- Palm Beach County agrees that some ambiguity existed during the initial phases of NSP1 implementation. We agree with HUD on the four cases to be reimbursed in the amount of $24,090. The County will reimburse the NSP1 account on August 1, 2011. The cases to be reimbursed are shown below.

#	Loan Number	Sales price in excess of discounted price
1	1-0600-01217091	$ 1,900.00
2	1-0600-00330102	$ 3,850.00
3	1-0600-00210101	$ 7,920.00
4	1-0600-01124092	$10,420.00
	Total	**$24,090.00**

Comment 2

***Excess Disbursed Funds*-the amount of funds disbursed for four home buyers exceeded the amount authorized by the mortgage agreement. Additional repair cost was approved and disbursed by the County but the homebuyers' mortgage was not increased.**

HUD's Recommendation- The County should implement corrective measures to remedy the one loan in which disbursed NSP1 funds exceeded the authorized mortgage or reimburse the NSP1 Program $8,836 from non-Federal funds.

County Response- All disbursements have been rectified and Palm Beach County has since established an internal process to insure final funding amounts match disbursements. Palm Beach County wishes to point out that in the four instances cited, the increases in funding was a result of the need to undertake required rehabilitation of the properties. This generally requires a mortgage modification. It is customary to file and record these modifications only after all of the work associated with the property's rehabilitation has been completed. This alleviates the necessity to prepare and file additional modifications to the mortgages. On April 6, 2011, the outstanding mortgage modification for loan # 1-0600-00726101 in the amount of $8,836.00 was recorded. We agree that policy and procedures (PPMs) are necessary to ensure staff has delineated processes for adherence to NSP (HUD) guidelines.

The Redevelopment Activity Did Not Have an Agreement

Comment 2

***Redevelopment Activity had no Agreement-* The County did not execute an agreement between the housing department and the facilities department. Local governments are subject to the same requirements as subrecipients therefore inter-department agreements should include the same provisions as those described at for the 24 CFR 570.503(b).**

HUD's Recommendation- Execute an agreement between HCD and Facilities which complies with 24 CFR 570.503(b).

County Response:- Palm Beach County is now preparing a Memorandum of Understanding between the Palm Beach County Department of Housing and Community Development (HCD) and the Palm Beach County Facilities Development and Operations Department (FDO) for the renovation of the homeless resource center project. The Memorandum of Understanding will cover the design and construction services associated with the use of NSP1 funds. The Memorandum of Understanding will be executed by May 15, 2011.

In regard to the acquisition of the vacant units at this facility as funded under NSP1, it should be noted that HCD did not request FDO's involvement in the acquisition process in the same manner as with the design and renovation work.

Accordingly, the Memorandum of Understanding being prepared does not include the already completed acquisition process as explained below.

FDO participated in the process as a County department under the direction of County Administration as did the County Attorney's office on legal matters, and as did the County's outside consultant. For example, FDO obtained appraisals for HCD, and assisted with its staff's expertise at the closing that was performed by a private title company. HCD performed key functions in the acquisition process as evidenced by the preparation and/or issuance of documents relevant to accomplishing the acquisition of the vacant units at the facility. For example, HCD performed the following:

- Prepared the Board of County Commissioners' agenda item to authorize the acquisition.
- Drafted the Purchase and Sale Agreements to acquire the properties.
- Signed notices and letters required under the Uniform Relocation Act to the parties from whom properties were acquired (such as letter of interest, offer letter, notice of eligibility).
- Prepared funds wire transfer requests for closings.

FINDING #2- <u>THE COUNTY DID NOT REPORT ACCURATE NSP1 PROGRAM INCOME TO HUD.</u>

Comment 2

***Program Income-* The County did not report accurate and timely program income in the HUD system as required by Federal regulations and did not use its earned program income before drawing down additional NSP1 funds.**

HUD's Recommendation- (1) The County should use the $211,952 in program income earned before drawing down additional NSP1 funds. **(2)** Develop and implement policies and procedures to ensure that it will report accurate program income information in the HUD system and use the program income before drawing down additional NSP funds.

County's Response- The $211,952 in program income earned through the quarter ending December 31, 2010 and after, will be used before drawing down additional NSP1 funds. The County acknowledges that the amount of program income earned was inaccurately reported in DRGR. This was due to an error in inputting the information. Using the County's AMS Advantage Financial System (Advantage) the County does have adequate controls in place to ensure that NSP program income is accurately received, deposited, tracked and used in accordance with Federal guidelines. A separate fund has been set up in Advantage to account for all NSP financial transactions, including those associated with program income.

Palm Beach County is now in the process of developing policies and procedures which will provide proper guidance on the reporting and expending of program income.

FINDING #3- <u>THE COUNTY DID NOT SUFFICIENTLY SUPPORT NSP2 ADMINISTRATIVE EXPENDITURES.</u>

***Administrative expenditures were not supported:* the County did not maintain documentation to sufficiently support the administrative expenditures recorded in its financial system. No documentation existed to support workers compensation and indirect cost and the County did not ensure that documentation supported the salary and benefit charges. Additionally, the County's financial system did not disclose accurate financial results of the NSP2 program. This led to a $10,000 drawdown of unsupported NSP2 funds.**

HUD's Recommendation- (1) County should provide documentation to support the $10,000 used to pay workers compensation **or** reimburse the NSP1 Program $10,000 from non-Federal funds. **(2)** Provide documentation to support the fiscal year 2011 indirect cost expenditure before it draws down NSP2 funds for reimbursement**. (3)** Determine the salary and benefit amounts for the applicable programs worked on by the employees and take corrective actions to report accurate salary and benefit amounts for the period. **(4)** Develop and implement PPM to ensure that (a) sufficient documentation is maintained to support budgeted cost items like indirect cost and workers compensation, and (b) accurate salary and benefit amounts are charged to the NSP2 program.

***County Response:-* (1)**Palm Beach County reimbursed the NSP2 program $10,000 from non-Federal funds on March 2, 2011 and documentation of this transaction

Comment 3

has been provided to the HUD Inspector General. HCD will now require County Departments that assess and post annual budgetary fees to provide detailed documentation to support the assessed amount that will be maintained in applicable grant files. **(2)** The County will not assess or request NSP2 funds for

Comment 2

reimbursement for indirect cost expenditures without detailed supporting documentation. To date, the NSP2 grant program has not been charged an indirect cost amount for FY2011. **(3)** The salary and benefit amounts for the

Comment 2

quarter ending September 2010 have been calculated and corrective reporting measures will be taken. The results will be reflected in the June 2011 Quarterly Report. **(4)** Policies and procedures will be developed and implemented to ensure:

Comment 2

1. Sufficient support documentation is available and kept in HCD grant files to support all budgeted cost items like indirect cost and workers compensation. Additionally, the County department responsible for assessing and allocating indirect costs is in the process of revising how

Comment 2

grant programs are charged and will provide detailed support documentation for audit purposes when the expense is posted.

2. We have revised our procedure to ensure that salary and benefit charge-offs to the NSP2 and other grant programs are accurate. Additionally, a tracking system will be used to ensure all timesheets used to charge-off salary/benefit amounts are received from appropriate staff and that all charge-offs are processed. To ensure accurate data transfer and calculation, copies of timesheets will now be included with the documentation used to support salary/benefit charge-off entries. This information will be reviewed by HCD fiscal support staff, HCD management and the County's Finance department.

Palm Beach County is excited to be able to provide assistance to its residents under the NSP1 and NSP2 Programs. We have recognized the impact of these two programs on reducing the volume of foreclosed homes in Palm Beach County as well as providing an opportunity for eligible low- and moderate-income homes to be able to afford housing. We strive to implement the NSP Programs in a manner which meets the Federal and the requirements of the Notices. Please contact me at (561) 233-3602 for further clarification and discussion on this matter.

Sincerely

Edward W. Lowery

Edward W. Lowery, Director

Cc: Shannon LaRocque-Baas, Assistant County Administrator
Kilah White, Assistant Regional Inspector General for Audit
Elena M. Escovar, Planning Manager
Journey Beard, Manager Contract Development and Quality Control
Amin Houry, Technical Services Coordinator
Shairette Major, Fiscal Manager I
Carol Eaddy-Langford, Manager Mortgage and Housing Assistance

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OIG Evaluation of Auditee Comments

Comment 1: The County agreed with the conflict-of-interest issue for 8 of the 10 loans and agreed to refund the NSP1 program for the $1,335,310 associated with the 8 loans by August 1, 2011. It asked OIG to reconsider its position on two loans (#1-0600-00920101 and #1-0600-01125091) totaling $393,711. For loan #1-0600-00920101, the County reasoned that the borrower is not an employee of the Board of County Commissioners, but an employee of the Clerk and Comptroller. For loan #1-0600-01125091, the County reasoned that the co-borrower was not a County employee at the time of loan application and funding approval.

HUD regulations at 24 CFR 570.611(b), (c), and (d) state that no persons defined as a covered person, who exercise or have exercised any functions or responsibilities or are in a position to gain inside information with respect to CDBG activities, may obtain a financial interest or benefit from a CDBG-assisted activity for themselves or those with whom they have business or immediate family ties, during their tenure or for 1 year thereafter. A covered person is defined as a person who is an employee, agent, consultant, officer, or elected or appointed official of the grantee, designated public agencies, or subrecipients. HUD may grant an exception to the provision on a case-by-case basis when the grantee's written request has satisfactorily met the threshold requirements. For loan #1-0600-00920101, the homebuyer is an employee of the Clerk and Comptroller, which is an entity of the County. Thus, the home buyer is a County employee and is defined as a covered person under 24 CFR 570.611(c). For loan #1-0600-01125091, the loan closing occurred November 25, 2009. The loan file contained a verification of employment from the County dated November 10, 2009, verifying that the co-borrower was a County employee. Given that the co-borrower was a County employee before loan closing, the co-borrower is a covered person under 24 CFR 570.611(c). In addition, since the County became aware that the co-borrower was a County employee before closing, it should not have proceeded to close until HUD granted a waiver.

HUD agreed that the home buyers in both loans are considered covered persons under HUD regulations and therefore the County needed to obtain HUD's waiver of the conflict of interest provision. The County did not request the required waiver from HUD and therefore must reimburse the NSP1 program the costs associated with the 10 loans, totaling $1,719,021.

Comment 2: The County agreed with the findings and recommendations to (1) repay the NSP1 program for the identified ineligible costs, (2) amend the difference between the disbursed and the funded amount for one home buyer, (3) execute an agreement between the housing department and the facilities department, (4) use program income before drawing down additional NSP1 funds, (5) ensure that all requests for NSP2 reimbursements are supported by detailed documentation, (6) correct the reporting for the NSP2 salaries and benefits, and (7) implement policies and procedures to address the identified conditions.

By taking the above measures and implementing procedures to address the recommendations, the conditions identified in the findings will be corrected and future incidents may be prevented.

Comment 3: The County indicated that it had reimbursed the NSP2 program $10,000 for the unsupported workers compensation cost on March 2, 2011, and provided documentation to the OIG. In addition, it will develop and implement policies and procedures to ensure that sufficient documentation is maintained to support budgeted cost items like workers compensation.

The County provided documentation which supported that $10,000 was refunded to the NSP2 program in the County's financial accounts. Additional documentation is required to support that the entries in the financial system are correct and the $10,000 refund came from non-Federal funds.

Appendix C

LIST OF LOANS REVIEWED WITH ASSOCIATED DEFICIENCIES AND INELIGIBLE COSTS

#	Loan number	Date closed	Conflict of interest	Property purchased without discount	Excess disbursed funds	Ineligible costs (a)
1	1-0600-00630102	06/30/2010	X			$ 208,000
2	1-0600-00520101	05/20/2010			X (c)	
3	1-0600-00520101	05/20/2010	X			$ 163,400
4	1-0600-00409101	04/09/2010	X			$ 184,090
5	1-0600-00726101	07/26/2010			X	$ 8,836
6	1-0600-01128091	12/28/2009		X (b)		
7	1-0600-01125091	11/25/2009	X			$ 196,098
8	1-0600-01124092	11/24/2009		X		$ 10,420
9	1-0600-01029101	10/29/2010	X			$ 150,000
10	1-0600-01217091	12/17/2009		X	X (c)	$ 1,900
11	1-0600-01214091	12/14/2009	X	X (d)		$ 117,713
12	1-0600-00920101	09/20/2010	X			$ 197,613
13	1-0600-00630101	06/30/2010	X			$ 189,000
14	1-0600-00330102	03/30/2010		X		$ 3,850
15	1-0600-00129101	01/29/2010	X			$ 212,800
16	1-0600-00210101	02/10/2010		X		$ 7,920
17	1-0600-01210091	12/10/2009	X	X (d)		$ 100,307
18	1-0600-00505101	05/05/2010			X (c)	
	Total		10	7	4	**$1,751,947**

Notes:

(a) Costs were calculated using the expenditure report from the County's financial system as of December 7, 2010.

(b) There was no questioned cost associated with the deficiency since the County transferred the related expenditures from the NSP1 fund to another funding source to address an audit finding cited by the County's Internal Audit Office for the same issue.

(c) There was no questioned cost associated with the deficiency since the County provided documentation to remedy the discrepancy after we disclosed the issue during our audit.

(d) There was no questioned cost associated with the deficiency since we questioned the entire expended amount because the home buyer was one of the County employees identified during the audit.