



Issue Date April 8, 2011

Audit Report Number 2011-AT-1006

TO: José R. Rivera, Director, Community Planning and Development, San Juan Field Office, 4ND

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

SUBJECT: The Municipality of Mayaguez, PR, Did Not Ensure Compliance With HOME Program Objectives

HIGHLIGHTS

What We Audited and Why

We audited the Municipality of Mayaguez (Municipality) HOME Investment Partnerships Program (HOME). We selected the Municipality for review as part of our strategic plan, based on the amount of HOME funds approved. The objectives of the audit were to determine whether the Municipality met program objectives in its HOME-funded activities and maintained its financial management system in compliance with U.S. Department of Housing and Urban Development (HUD) requirements.

What We Found

The Municipality disbursed more than \$4.4 million for two activities that did not meet HOME program objectives and more than \$2.8 million for an additional activity for which it could not support its compliance with HOME program objectives. As a result, HUD had no assurance that funds were used solely for eligible purposes and that HOME program objectives were met.

The Municipality's financial management system did not support the eligibility of \$1.5 million in disbursements, and did not account for more than \$23,000 in HOME receipts. In addition, the Municipality failed to disburse HOME funds in a timely manner and provided HUD with inaccurate information. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for authorized purposes.

What We Recommend

We recommend that the Director of the San Juan Office of Community Planning and Development require the Municipality to repay more than \$4.7 million for ineligible expenditures that did not result in benefits to the HOME program. The Director should also require the Municipality to provide all supporting documentation to demonstrate the allocability and eligibility of more than \$2.5 million in disbursements. The Municipality should also reprogram and put to better use more than \$900,000 in unexpended funds for an activity that did not meet HOME program objectives.

The Director should also require the Municipality to develop and implement an internal control plan to ensure that the HOME program has (1) a financial management system that complies with HUD requirements and (2) controls and procedures which ensure that HOME requirements are followed and accurate information is reported to HUD.

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 discussed the findings with HUD and the Municipality during the audit and at the exit conference on February 22, 2011. The Municipality provided its written comments to the draft report on March 7, 2011. In its response, the Municipality generally disagreed with the findings.

The complete text of the Municipality's response, along with our evaluation of that response, can be found in appendix B of this report. Attachments to the Municipality's comments were not included in the report but are available for review upon request.

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BACKGROUND AND OBJECTIVES

The HOME Investment Partnerships Program (HOME) is authorized under Title II of the Cranston-Gonzalez National Affordable Housing Act as amended. The U.S. Department of Housing and Urban Development (HUD) allocates funds by formula to eligible State and local governments for the purpose of increasing the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families. State and local governments that become participating jurisdictions may use HOME funds to carry out multiyear housing strategies through acquisition, rehabilitation, new housing construction, and tenant-based rental assistance.

Participating jurisdictions are required to commit HOME funds within 24 months and expend them within 5 years after the last day of the month in which HUD notifies the participating jurisdiction of HUD's execution of the HOME agreement. Participating jurisdictions draw down HOME funds through HUD's Integrated Disbursement and Information System (information system). HUD's information system is also used to monitor and track HOME commitments, program income, repayments, and recaptured funds, among other things.

The Municipality of Mayaguez (Municipality) is the sixth largest participating jurisdiction in Puerto Rico, for which HUD has approved more than \$3.5 million in HOME funds during the past 3 fiscal years. HUD's information system reflected expenditures exceeding \$1.02 million during the fiscal year ending June 30, 2009, for the following activities:

Activity type	Amount expended
Home-buyer assistance	\$453,114
Community housing development organizations (CHDO)	409,963
Tenant-based rental assistance	82,715
Planning and administration	66,527
Homeowner assistance - new construction	<u>12,957</u>
Total	<u>\$1,025,278</u>

The Municipality's Department of Housing and Federal Funds was responsible for managing the HOME program. Its books and records were maintained at #123 South Ramon E. Betances Street, Mayaguez, PR. We audited the Municipality's HOME program as part of the HUD Office of Inspector General's (OIG) strategic plan.

The objectives of the audit were to determine whether the Municipality met HOME program objectives and maintained its financial management system in compliance with HUD requirements.

RESULTS OF AUDIT

Finding 1: The Municipality Did Not Meet HOME Program Objectives

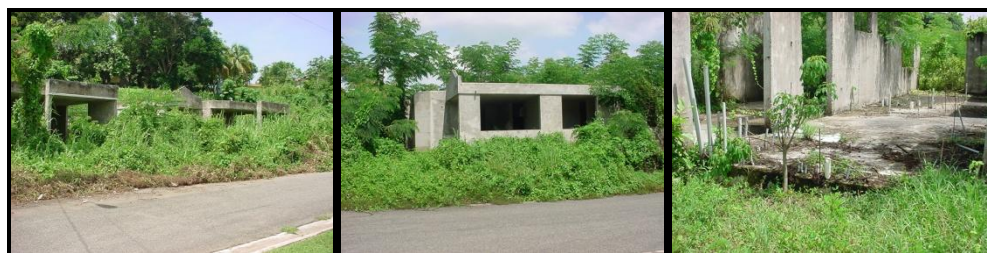
The Municipality disbursed more than \$4.4 million for two activities that did not meet HOME program objectives and more than \$2.8 million for an additional activity for which it could not support its compliance with HOME program objectives. We attribute the noncompliance to the inadequate monitoring of HOME-funded activities and the Municipality's unfamiliarity with HUD requirements. As a result, HUD had no assurance that funds were used solely for eligible purposes and that HOME program objectives were met.

HOME Objectives Not Met

HUD's regulations at 24 CFR (Code of Federal Regulations) 92.1 state that HOME funds are allocated to participating jurisdictions to strengthen public-private partnerships and to expand the supply of decent, safe, sanitary, and affordable housing for low- and very low-income families. Regulations at 24 CFR 92.205(e) provide that a HOME-assisted activity that is terminated before completion, either voluntarily or otherwise, constitutes an ineligible project and any HOME funds invested must be repaid to the participating jurisdiction's treasury account.

Contrary to HUD's regulations, the Municipality failed to ensure that two activities met HOME objectives.

Estancias del Rio housing project - In July 1993, the Municipality initially funded through a community housing development organization (CHDO) the construction of a 121-unit housing project named Estancias del Rio. The agreement with the CHDO indicated that the construction should have been completed in August 1997. More than 17 years had elapsed since the housing project was initially funded, and the Municipality had completed only 22 (18 percent) of the proposed housing units, of which 21 were occupied.



Partial view of incomplete and abandoned units within the Estancias del Rio housing project



Aerial view of Estancias del Rio, source Google maps.

The CHDO responsible for the development of Estancias del Rio defaulted on the construction loan, and in June 2006, the bank sued the CHDO for the collection of monies, foreclosure of pledge agreement, and breach of contract, among other things. As a result, the construction work stopped. In an attempt to restart the project, the Municipality disbursed \$400,000 in HOME funds in April 2009 to pay off the outstanding construction loan. In May 2010, the Municipality delegated to another CHDO the completion of the project, reduced the scope of the project to 85 units, and committed an additional \$1.2 million in HOME funds.

The Municipality disbursed more than \$4.43 million in HOME funds and failed to ensure the timely completion of the activity. More than 17 years had elapsed, and the project had not been completed. As a result, HUD had no assurance that the activity provided the intended benefits and met HOME objectives. HUD informed us that providing additional HOME funds to a project that the Municipality had not been able to complete in more than 17 years was inconsistent with HOME regulations. Therefore, the Estancias del Rio housing project did not comply with HOME requirements, and the Municipality needs to return all of the funds disbursed. In a letter, dated October 27, 2010, HUD informed the Municipality of its decision, disallowing all funds disbursed, requesting the reimbursement of more than \$4.3 million, and prohibiting any additional funding to the housing project.¹

The Municipality contended that HUD requirements did not establish timeframes for when a project should be completed. Thus, it believed that the Estancias del Rio housing project complied with program requirements and that the development of the housing project should continue. This was not an acceptable explanation for

¹ During the audit, we consulted HUD headquarters about the propriety of using \$400,000 in HOME funds to pay off the defaulted construction loan. In its response, HUD informed us and the San Juan HUD CPD field office that the Estancias del Rio housing development was not compliant with program requirements. As a result of our review and inquiries, HUD requested the reimbursement of all funds.

not completing this activity in a timely manner and allowing it to go on for more than 17 years. HUD's regulations at 24 CFR 92.500(d) requires participating jurisdictions to expend HOME funds within 5 years from the execution of the HOME program agreement. Regulations at 24 CFR 92.2 define commitments to specific local projects as those that can be reasonably expected to commence within 12 months of the agreement date.

The Municipality did not adequately manage this activity to ensure that it was carried out in a timely manner and that funds were used in accordance with all HOME requirements as provided at 24 CFR 92.504(a). We attribute this deficiency to the inadequate planning and capacity of the CHDO. For example, the Municipality selected three different CHDOs to undertake the activity, but it had not been able to complete the project in more than 17 years. In addition, one of the CHDOs did not have the capacity to repay and defaulted on the project construction loan and selected a contractor that could not provide a payment and performance bond. The Municipality should discontinue this activity and reimburse more than \$4.43 million in HOME disbursements. In addition, \$906,091 in unexpended HOME funds, as reflected in HUD's system, should be reprogrammed and put to better use for other eligible efforts.

Home-buyer assistance activity #1141 - This activity was initially funded in July 2007, providing \$10,000 in HOME assistance to a participant for the acquisition of a home. In April 2009, the Municipality withdrew from HUD the full amount, but it had not disbursed any funds toward the acquisition of the home. Thus, the Municipality failed to ensure that the activity provided the intended benefits and met HOME objectives.

Regulations at 24 CFR 92.502(c)(2) state that HOME funds withdrawn from the treasury account must be expended for eligible costs within 15 days. Any unexpended drawdowns must be returned to HUD. Contrary to HUD's regulations, the Municipality did not disburse the funds it withdrew from its HOME treasury account and did not return to HUD the unexpended drawdown.

The HOME program supervisor informed us that one of the parties involved in the transaction died and the funds remained in the Municipality's bank account. The official also informed us that she was not aware of HUD's timeframe requirements for disbursing drawdowns. This was not an acceptable explanation for not performing an integral component of its HOME program responsibilities. Thus, the Municipality did not adequately manage this activity to ensure that it was carried out in a timely manner and that funds were used in accordance with all program requirements. The Municipality should not continue with this activity and must reimburse \$10,000 in HOME disbursements.

HOME Objectives Not Supported

Villas de Felisa housing project - The Municipality disbursed more than \$2.4 million in HOME funds for the acquisition of approximately 24.59 acres of land and the development of a 272-unit housing project named Villas de Felisa.² Although the construction of the project was completed in April 2002, HUD's information system showed it as an open activity with the final draw made in February 2001. The activity remained open in HUD's information system because the Municipality did not have the required information on participants, including information to support that income eligibility requirements had been met. As a result, HUD had no assurance that this activity increased the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families and that HOME objectives were met.

HUD's regulations at 24 CFR 92.1 state that HOME funds are allocated to participating jurisdictions to strengthen public-private partnerships to expand the supply of decent, safe, sanitary, and affordable housing to low- and very low-income families. Regulations at 24 CFR 92.203(a) provide that participating jurisdictions must determine that each participant family is income eligible.

Contrary to HUD's regulations, the Municipality did not take the appropriate measures to ensure that subsidized units were occupied by eligible participants. The Municipality could not support the income eligibility of the participants as required by HUD.³ Therefore, HUD lacked assurance of the allowability and allocability of more than \$2.4 million charged to the HOME program.

The Municipality also did not use or develop all of the 24.59 acres of land acquired for the Villas de Felisa housing project. According to Municipality records, only 18.64 acres of land were developed for the housing project. Therefore, approximately 6.48 acres of land had remained unused since being acquired in 1998 without providing the intended benefit of expanding the supply of decent, safe, sanitary, and affordable housing for low- and very low-income families. HUD's regulations at 24 CFR 205(a)(2) state that acquisition of vacant land must be undertaken only with respect to particular projects intended to provide affordable housing. Because the land did not provide affordable housing, it did not comply with HOME objectives. Contrary to HUD's regulations, the Municipality disbursed more than \$273,000 for ineligible purposes.⁴

² The Municipality disbursed an additional \$420,000 in Community Development Block Grant funds for this activity.

³ A September 2007 HUD monitoring report disclosed a similar deficiency, but it had not been resolved.

⁴ The ineligible amount represents the proportional price paid for the unused land (6.48 acres) based on the total purchase price for the 24.59 acres of land acquired [(\$1,036,000/24.59 acres) x 6.48 unused acres].

The Municipality failed to ensure that each participant family living at Villas de Felisa was income eligible and that HOME objectives were met. This noncompliance occurred because the Municipality disregarded HUD requirements. Therefore, more than \$2.56 million in disbursements was unsupported, and more than \$273,000 paid for the unused property was ineligible.

Conclusion

The Municipality failed to ensure that activities met HOME objectives. This deficiency occurred because the Municipality did not properly monitor HOME-funded activities and was not fully aware of HUD requirements. As a result, HUD had no assurance that funds were used solely for eligible purposes and that HOME program objectives were met. The Municipality paid more than \$4.7 million for activities that did not provide the intended benefits. In addition, it failed to support the allowability and allocability of more than \$2.56 million.

Recommendations

We recommend that the Director of the San Juan Office of Community Planning and Development

- 1A. Require the Municipality to reimburse its HOME treasury account or HUD, as appropriate, from non-Federal funds \$4,433,035 for disbursements associated with two activities that did not meet HOME program objectives.⁵
- 1B. Require the Municipality to reprogram and put to better use \$906,091 associated with unexpended funds for the Estancias del Rio housing project.
- 1C. Require the Municipality to submit all supporting documentation showing the allowability and allocability of \$1,062,991 disbursed for participant families at the Villas de Felisa housing project or reimburse this amount to its HOME treasury account or HUD, as appropriate, from non-Federal funds.⁶
- 1D. Require the Municipality to reimburse its HOME treasury account or HUD, as appropriate, from non-Federal funds \$273,009 paid for land acquired for the Villas de Felisa housing project that did not provide the intended benefits.
- 1E. Require the Municipality to establish and implement appropriate monitoring procedures to ensure HOME requirements and objectives are met.

⁵ Total disbursements of \$4,444,697 were adjusted to consider \$11,662 questioned in recommendation 2B.

⁶ Total disbursements of \$2,836,000 were adjusted to consider \$1,500,000 questioned in recommendation 2A and \$273,009 ineligible in recommendation 1D.

- 1F. Provide training and technical assistance to the Municipality's HOME program staff on timeliness requirements for disbursements and completion of activities.

Finding 2: The Municipality’s Financial Management System Did Not Comply With HUD Requirements

The Municipality’s financial management system did not support the eligibility of \$1.5 million in disbursements, and did not account for more than \$23,000 in HOME receipts. In addition, it failed to disburse HOME funds in a timely manner and provided HUD with inaccurate information. These deficiencies occurred because the Municipality lacked written procedures and controls to ensure compliance with HUD requirements. As a result, HUD lacked assurance that funds were adequately accounted for, safeguarded, and used for authorized purposes.

Unsupported Program Disbursements

Regulations at 24 CFR 92.205(a) allow disbursements for reasonable expenditures associated with the HOME program that are supported with records that enable HUD to determine that HOME requirements were met. In addition, 24 CFR 508(a)(3)(ii) requires participating jurisdictions to maintain records demonstrating the source and application of funds for each project including supporting documentation in accordance with 24 CFR 85.20.

The Municipality did not provide documentation supporting the reasonableness, allowability, and allocation of \$1.5 million charged to the HOME program, associated with the Villas de Felisa housing project. It paid for construction work without progress/engineering certifications, cost descriptions, or other support showing the work or service that was performed. A Municipality official informed us that the disbursements made to the developer of the housing project were based on the contract agreement. No detailed documentation was provided by the contractor. Therefore, HUD lacked assurance that funds were used for authorized purposes.

Inaccurate Accounting Records

Regulations at 24 CFR 85.20(a) require participating jurisdictions to maintain fiscal controls and accounting procedures sufficient to permit the preparation of reports and the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.

The Municipality’s accounting records were not accurate, current, and complete. They did not reflect complete financial information on HOME activities and did not permit the adequate tracing of program expenditures. For example, the

expenditures shown in the Municipality's accounting records did not agree with amounts reflected in HUD's information system.

Activity type	HUD's information system	Accounting records	Difference
Estancias del Rio	\$4,096,677	\$4,085,015	\$(11,662)
Home-buyer assistance (as of April 30, 2010)	\$387,402	\$376,000	(11,402)
Tenant-based rental assistance (as of June 30, 2008)	\$82,715	\$81,917	(798)
Total			\$(23,862)

The Municipality could not explain the discrepancies and could not account for more than \$23,000 drawn from HUD for various HOME activities.

HOME Funds Not Disbursed in a Timely Manner

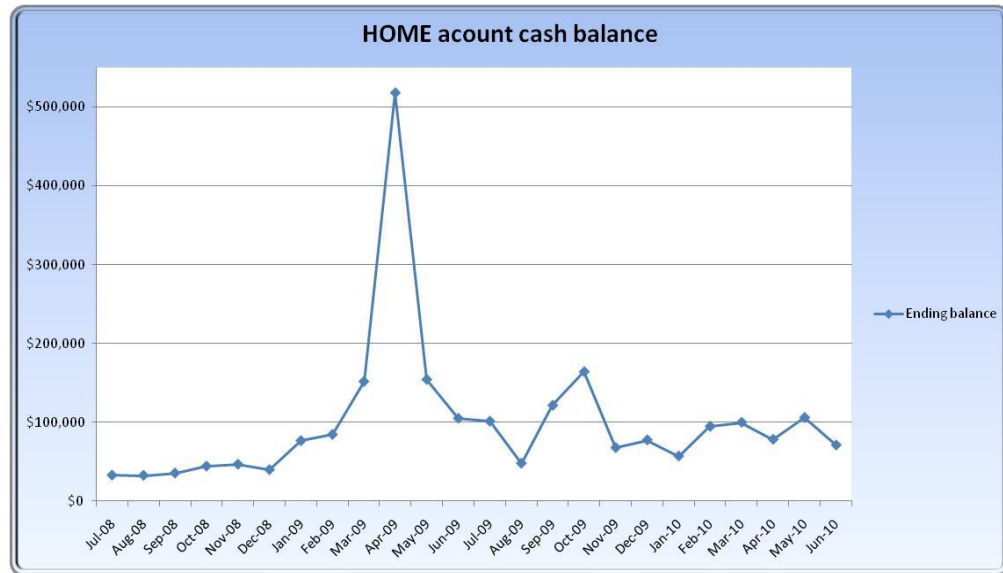
The Municipality withdrew more than \$1.7 million in HOME funds from its treasury account between July 1, 2008, and April 30, 2010. Regulations at 24 CFR 92.502(c)(2) state that HOME funds drawn down from the treasury account must be expended for eligible costs within 15 days. Any unexpended drawdowns must be returned to HUD.

Contrary to HUD's regulations, the Municipality failed to disburse drawdowns totaling more than \$470,000 (27 percent) in HOME funds within 15 days. Further, it did not return any of the HOME funds to HUD and consistently maintained a high cash balance in its bank account.

Voucher number	Activity number	Date of drawdown deposit	Date of disbursement	Days elapsed between deposit and disbursement dates
5092780	1057	Apr. 14, 2010	Apr. 30, 2010	16
5060693	804	Feb. 2, 2010	Feb. 23, 2010	21
1659119	219	Apr. 8, 2009	May 07, 2009	29
1659119	219	Apr. 8, 2009	May 07, 2009	29
5064784	1307	Feb. 11, 2010	Mar. 12, 2010	29
5078366	872	Mar 15, 2010	Apr. 22, 2010	38
1655352	219	Mar. 27, 2009	Aug. 20, 2009	146
5004751	1281	Sept. 9, 2009	Jul. 07, 2010	301
1663576	1141	Apr. 21, 2009	Not disbursed	n/a

Regulations at 24 CFR 92.502(c)(3) require that HOME funds in the participating jurisdiction's local bank account be disbursed before additional grant funds are

requested. The Municipality consistently maintained a high cash balance in its bank account. The Municipality’s June 30, 2010, bank statement reflected a cash balance of more than \$70,000, and the Municipality maintained a monthly average balance of more than \$100,000 during the 24-month period ending June 30, 2010.



The independent public accountant report included similar cash management deficiencies during the past 3 years. However, the deficiency continued to exist.

Inaccurate Reporting

Participant jurisdictions are required by 24 CFR 92.500(d) and 92.502 to commit HOME funds within 24 months of their allocation and report commitment information in HUD’s information system. HUD’s regulations at 24 CFR 92.2 define “commitment” as (1) an executed, legally binding agreement with a State recipient, a subrecipient, or a contractor to use a specific amount of HOME funds to produce affordable housing or provide tenant-based rental assistance or an executed written agreement reserving a specific amount of funds to a CHDO or (2) having met requirements to commit to a specific local project, which also requires that a written, legally binding agreement be executed with the project or property owner. HUD Notice 07-06 dated June 1, 2007, also requires that the signatures of all parties be dated to show the execution date.

The Municipality reported in HUD’s information system that it had committed more than \$35,000 in HOME funds, although it did not have executed agreements with the recipients. The actual commitments occurred between 266 and 1,170 days after the funding date. Therefore, the funds were not reported as committed in accordance with HUD requirements.

Activity number	Reported commitment amount in HUD's information system	Funding date in HUD's information system	Actual agreement date	Days elapsed between agreement and reporting dates
896	\$12,975	Sept. 8, 2005	Nov. 21, 2008	1,170
658	<u>\$22,752</u>	Nov. 25, 2003	Aug. 17, 2004	266
Total	<u>\$35,727</u>			

We also found 11 instances in which the Municipality reported in HUD's information system the commitment of more than \$1.6 million in HOME funds between 1 and 76 days after the grant agreement was executed. Therefore, the funds were not reported as committed in accordance with HUD requirements.

Activity number	Reported commitment amount in HUD's information system	Funding date in HUD's information system	Actual agreement date	Days elapsed between reporting and agreement dates
1345	\$40,000	Jan. 25, 2010	Nov. 10, 2009	76
1337	\$40,000	Oct. 23, 2009	Aug. 21, 2009	63
1290	\$50,000	June 12, 2009	Apr. 24, 2009	49
1254	\$40,000	Mar. 25, 2009	Mar. 11, 2009	14
1342	\$40,000	Nov. 24, 2009	Nov. 10, 2009	14
1280	\$40,000	May 26, 2009	May 14, 2009	12
1299	\$46,000	July 24, 2009	July 16, 2009	8
1298	\$40,000	July 24, 2009	July 16, 2009	8
1339	\$40,000	Nov. 06, 2009	Oct. 30, 2009	7
1340	\$40,000	Nov. 06, 2009	Oct. 30, 2009	7
1351	<u>\$1,206,541</u>	May 28, 2010	May 27, 2010	1
Total	<u>\$1,622,541</u>			

HUD's information system contained additional inaccurate information concerning the Municipality's HOME activities. Regulations at 24 CFR 92.502(d) require participant jurisdictions to report in HUD's information system the status of each activity assisted with HOME funds. However, the Municipality did not always report accurate information associated with its activities. Three activities were shown as open activities with unexpended funds, although the construction was completed in November 2009. A Municipality official informed us that the activities were not closed because it planned to use the remaining unexpended \$2,008 on other activities. This was not an acceptable explanation for not performing an integral component of its HOME program responsibilities. HUD's regulations at 24 CFR 92.502(d) also state that participant jurisdictions need to

enter project completion information within 120 days from the final drawdown. The Municipality must close these activities and reprogram the \$2,008 in unexpended funds.

The inaccurate data compromised the integrity of HUD's information system and the degree of reliability HUD could place on the data for monitoring commitments and compiling national statistics on the HOME program. Management must improve its controls to ensure the accuracy of its reported accomplishments and that it complies with HUD requirements.

Lack of Procedures and Controls

The lack of program controls and procedures also contributed to the Municipality's improper administration of HOME funds. Controls and procedures implemented by the Municipality were not sufficient and adequate to provide HUD assurance that all funds were properly tracked, reported, and used in accordance with HUD requirements. For example, the Municipality's written procedures did not provide for controls that ensured the adequate reporting or monitoring of commitment information reported in HUD's information system. In addition, the procedures did not provide for controls that ensured the timely use of HOME drawdowns. Management must revise and implement its controls and procedures to ensure the proper administration of program receipts and improve the accuracy of data reported to HUD.

The lack of program controls and procedures has been pointed out in previous audits. Our previous audit of the Municipality's Community Development Block Grant and Section 108 Loan Guarantee Assistance program disclosed a number of compliance and financial management problems. Similarly the Municipality's most recent independent audit disclosed continuing noncompliance with HUD requirements.

Conclusion

Because the Municipality lacked adequate procedures and internal controls, it made ineligible and unsupported disbursements, could not account for funds drawn, did not disburse funds in a timely manner, and did not ensure the accuracy of commitments and other information entered into HUD's information system. The lack of established procedures to permit the tracing of HUD funds and ensure that they have not been used in violation of applicable statutes is a major concern. Management must improve its internal controls to ensure that HUD requirements are met and that it achieves HOME program goals.

Recommendations

We recommend that the Director of the San Juan Office of Community Planning and Development

- 2A. Require the Municipality to submit all supporting documentation showing the eligibility and propriety of \$1.5 million charged to the HOME program for the development of the Villas de Felisa housing project or reimburse the program from non-Federal funds.
- 2B. Require the Municipality to submit all supporting documentation showing the eligibility and propriety of \$23,862 drawn from HUD or reimburse the HOME program from non-Federal funds.
- 2C. Require the Municipality to deobligate in HUD's information system, then reprogram and put to better use, \$2,008 associated with unexpended funds related to the completed activities.
- 2D. Require the Municipality to establish and implement adequate procedures to ensure that it disburses HOME funds for eligible activities within HUD's established timeframes.
- 2E. Require the Municipality to establish and implement adequate controls and written procedures to ensure that accurate commitment and activity information is reported in HUD's information system.
- 2F. Require the Municipality to review all grant agreements for each activity entered into HUD's information system and correct any inaccurate information, including funding amount, activity status, and funding type classification.
- 2G. Require the Municipality to develop and implement a financial management system that permits the tracing of HOME funds to a level which ensures that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes and that funds are drawn and used for their intended purpose only.

SCOPE AND METHODOLOGY

The objectives of the audit were to determine whether the Municipality met HOME program objectives and maintained its financial management system in compliance with HUD requirements. The financial requirements included the expenditure of HOME funds for eligible and supported project costs, reporting accurate and supported commitments in HUD's information system, and disbursing HOME funds within the established timeframes.

To accomplish our objectives, we

- Reviewed applicable HUD laws, regulations, and other HUD program requirements;
- Reviewed the Municipality's controls and procedures as they related to our objectives;
- Interviewed HUD, Municipality, developer, and CHDO officials;
- Reviewed monitoring, internal review, and independent public accountant reports;
- Reviewed the Municipality's files and records, including activity files and accounting records;
- Traced information reported in HUD's information system to the Municipality's records, including accounting records and executed agreements; and
- Performed site inspections of the activities.

HUD's information system reflected that the Municipality had 22 open HOME-funded activities as of April 30, 2010. We selected and reviewed four activities for which the last draw was more than a year earlier, with withdrawals totaling more than \$4.4 million. We also reviewed five activities that were funded on or before 2005 and for which the last draw was between 100 and 200 days old (before April 30, 2010), with withdrawals totaling more than \$108,000. We reviewed the nine activities in the sample to determine the status of activities for which HOME funds were disbursed but which reflected slow progress.

HUD's information system reflected that the Municipality committed more than \$1.05 million between July 1, 2008, and April 30, 2010. We selected for review a sample of commitments equal to or greater than \$40,000, which resulted in commitments of \$416,000 associated with 10 activities. We reviewed one additional commitment totaling more than \$1.2 million that was made on May 28, 2010, because the amount was significant. We reviewed these activities to determine whether the commitments reported to HUD were accurate and supported.

The Municipality drew down from HUD between July 1, 2008, and April 30, 2010, more than \$1.7 million in HOME funds. We selected and reviewed 12 withdrawals greater than or equal to \$35,000. We also reviewed eight withdrawals greater than \$5,500 made between January and April 2010 and reviewed two withdrawals based on the program year funding. A total of 22 withdrawals totaling more than \$900,000 (about 52 percent) were reviewed to determine whether the Municipality expended grant funds in accordance with HUD requirements.

To achieve our audit objectives, we relied in part on computer-processed data contained in the Municipality's database and HUD's information system. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing and found the data adequate for our purposes. The results of the audit apply only to the items selected and cannot be projected to the universe or population.

The audit generally covered the period July 1, 2008, through April 30, 2010, and we extended the period as needed to accomplish our objectives. We conducted our fieldwork from June through November 2010 at the Municipality's offices in Mayaguez, PR.

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

INTERNAL CONTROLS

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:

- Program operations - Policies and procedures that the audited entity has implemented to provide reasonable assurance that a program meets its objectives, while considering cost effectiveness and efficiency.
- Compliance with applicable laws and regulations and provisions of contracts or grant agreements - Policies and procedures that the audited entity has implemented to provide reasonable assurance that program implementation is in accordance with laws, regulations, and provisions of contracts or grant agreements.
- Safeguarding of assets and resources - Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded 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 Municipality failed to ensure that HOME activities met program objectives (see finding 1).
- The Municipality did not develop and implement a financial management system that complied with HUD requirements (see finding 2).

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	\$4,433,035		
1B			\$906,091
1C		\$1,062,991	
1D	273,009		
2A		1,500,000	
2B		23,862	
2C			2,008
Total	<u>\$4,706,044</u>	<u>\$2,586,853</u>	<u>\$908,099</u>

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 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 HUD implements recommendations 1B and 2D, funds will be available for other eligible activities consistent with HOME requirements.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



Estado Libre Asociado de Puerto Rico
Gobierno Municipal de Mayagüez
Departamento de Vivienda y Programas Federales



March 7th, 2011

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

Dear Mr. McKay:

Enclosed are the Municipality of Mayaguez's Comments in response to the OIG Audit Report Draft and supporting documents. Supporting documents have been digitalized for your inspection and enclosed in the Municipality's SkyDrive website. You will be invited to access this website by an e-mail to your electronic address. You may access the website from this moment on.

Access to this website has been granted to you, Mr. Michael A. Rivera, Assistant Regional Inspector General for Audit at the San Juan Field Office, Mr. German Perez, HUD OIG Senior Auditor and Mr. Jose R. Rivera, CPD Director for the Caribbean Field Office. You may download the Municipality's Comments and any of the supporting documentation from this site.

Originals are available for inspection at the premises of the Municipality's Department of Housing and Federal Programs. Hard copies of the supporting documentation will be sent upon request.

Should you need any additional information please contact the Department of Housing and Federal Programs at (787) 833-3160, or viviendama@coqui.net.

Cordially,

Ms. Edna Rodríguez Valentín, Esq.
Manager
Department of Housing and Federal Programs
Municipality of Mayaguez

MUNICIPALITY OF MAYAGUEZ
WRITTEN COMMENTS TO OIG'S AUDIT REPORT DRAFT
&
SUPPORTING DOCUMENTATION

Finding 1 -

The Municipality did not meet HOME Program Objectives

Finding 1A – HOME Objectives Not Met

Recommendation 1A

Require the Municipality to reimburse its HOME treasury account or HUD, as appropriate, from non-Federal funds \$4,302,360 for disbursements associated with two activities that did not meet HOME program objectives.



Municipality's Comments

The Municipality disagrees.

On November 22, 2010 the Municipality submitted a Request for Reconsideration of HUD's Determination on Estancias Del Rio Project to the Assistant Secretary for CPD, Ms. Mercedes Márquez and the Caribbean Field Office. A copy of this document was delivered at the San Juan Office of the OIG on December 16th, 2010.

This subject is still under the consideration of the Assistant Secretary. Supporting documentation for this request included the reasons for the project's delays, current cash flows and projected sales schedules, and the monthly progress reports up to November 2010. These documents evidenced the fact that the project is undergoing construction and was schedule to be completed within the 24 months.

The project has continued construction using the Developer's fee. Seven units are over 95% completed and will be sold within the next 15 days.

The Municipality wants to make perfectly clear that this matter is still under consideration of the office of Assistant Secretary for Community Planning and Development, Ms. Mercedes Marquez at HUD's Headquarters. The Municipality has formally presented to the Assistant Secretary Marquez a Request for Reconsideration of HUD's determination to disallow and request the reimbursement of all funds disbursed and prohibition of any additional funding.

Comment 1

Comment 1

Nevertheless, the Municipality will address the issues presented in this finding in order to be on record as to the disposition of such allegations.

OIG's contention

"The Municipality contended that HUD requirements did not establish timeframes for when a project should be completed. Thus, it believed that the Estancias del Rio housing project complied with program requirements and that the development of the housing project should continue. This was not an acceptable explanation for not completing this activity in a timely manner and allowing it to go on for more than 17 years."

HUD's regulations at 24 CFR 92.500(d) require participating jurisdictions to expend HOME funds within 5 years from the execution of the HOME program agreement. HUD's regulations at 24 CFR 92.500(d) require participating jurisdictions to expend HOME funds within 5 years from the execution of the HOME program agreement. Regulations at 24 CFR 92.2 define commitments to specific local projects as those that can be reasonably expected to commence within 12 months of the agreement date."

Municipality's Comments

The Municipality disagrees with the contention that it has not complied with the objective criteria established in 24 CFR 92.500(d). All funds committed to this project have been disbursed in compliance with the time frames established in cited regulation. The Municipality has also complied with the criteria established in 24 CFR 92.2. At the time funds were committed, the Municipality had reasonable expectation that the project would commence within the 12 months of the agreement date. The Municipality has indeed complied with cited regulation.

Cited regulations are not applicable to the term of construction. 24 CFR 92.500(d) clearly establishes terms to disburse funds and 24 CFR 92.2 establishes a subjective timeframe to commence projects, after funds are committed. In no way do these regulations refer to time limits for completion of projects. To apply cited regulations to the present facts is an incorrect interpretation of HUD's regulations.

A thorough revision of the Cranston Gonzalez Affordable Housing Act, as amended, reveals that Congress has not established a statutory time frame for completion of projects. If Congress intends to apply a time frame, it must do so by enacting legislation to such effect.

A thorough revision of 24 CFR 92 reveals that HUD has not approved any regulation establishing a term for completion of HOME assisted new construction projects. If HUD had intended to enact such a regulation it must do so in compliance with the Administrative Procedures Act.

None of this has happened. In consequence HUD's determination has no basis in law. This determination is arbitrary and capricious because it is not supported in the Law or Regulations that govern the HUD assisted activity in question.

A determination that declares a project not in compliance with HOME requirements which entails the return of all HOME funds disbursed is a serious matter that must be made in full compliance with the

Comment 1

applicable laws and regulations that govern such process. To dismiss the Municipality's contention that such a determination cannot be made based on statutes or regulations that do not exist, with a statement such as "this was not an acceptable explanation" is to provide a light treatment to a very serious question. In addition to the fact, that it places HUD in violation of the statutory requirement that any actions taken by an Administrative Agency must be based on a legal disposition authorizing such an action.

OLG's contention

"The Municipality did not adequately manage this activity to ensure that it was carried out in a timely manner and that funds were used in accordance with all HOME requirements as provided at **24 CFR 92.504(a)**. We attribute this deficiency to the inadequate planning and capacity of the CHDO. For example, the Municipality selected three different CHDOs to undertake the activity, but it had not been able to complete the project in more than 17 years. In addition, one of the CHDOs did not have the capacity to repay and defaulted on the project construction loan and selected a contractor that could not provide a payment and performance bond."

Municipality's Comments

The Municipality disagrees with the contention that it has not complied with the responsibilities stated in *24 CFR 92.2*. The evidence that the Municipality has indeed complied with the responsibilities for ensuring that HOME funds were used in accordance with all program requirements and written agreements and that it took all appropriate actions in each instance that performance problems arised is presented in the Brief History addendum of the Request for Reconsideration. In this document each performance problem faced by the project and the action taken by the Municipality is described in detail in a chronological manner.

All actions taken were adopted in accordance with the applicable statute or regulation including the selection of the new CHDOs when deemed necessary for the completion of the project.

As stated in the Brief History the new CHDO entered into a joint venture agreement with a private developer which agreed to provide an interim construction loan within 90 days after the execution of the grant agreement. The Municipality approved the joint venture and the request for additional funds based on a Subsidy Layering Analysis. Please refer to Subsidy Layering Analysis, Allocation of HOME funded costs of the original project. (grant agreement dated May 27th, 2010)

It is public knowledge that the banks were not granting construction loans at that moment because of the crisis in the financial and construction sectors of the economy. For this reason the private developer was unable to secure the interim construction loan within the 90 days provided in the joint venture agreement. New CHDO terminated the agreement with the private developer.

At that moment the new CHDO proposed and the Municipality approved that an alternate means of financing, was converting HOME funds allocations of \$2,212,678, (which were the funds expected to be available for this project), into a revolving fund for financing the completion of the construction. Please

Comment 1

refer to enclosed Revolving Fund and Cash Flow Estimates, Subsidy Layering Analysis-Project Liquidation and Assumptions for Subsidy Layering Analysis, Cash Flow and Sales Proceeds. (grant agreement dated September 17, 2010)

New CHDO requested and the Municipality approved an advance of \$233,000.25, or 34% of the developer's fee. New CHDO invested the developer's fee in the revolving fund, which in addition to the sales proceeds will be used for the construction of the housing units.

At project completion sales proceeds in an approximate amount of \$700,000 will be returned by new CHDO as program income.

In order for the project to be feasible, in the grant agreement dated May 27th, 2010, the subsidy analysis shows that the previously disbursed HOME funds were allocated to development subsidy and were used for land acquisition, site improvement, surcharged and infrastructure. Consequently, a "right down" was given to previously disbursed funds in order to reduce the total sales/value price of the housing unit to market value.

All supporting documentation that evidenced the fact that all HOME and interim construction loan funds disbursed in the Estancias del Rio project were spent in eligible costs was available for inspection during the audit period and was in fact inspected by the auditors.

OID's contention

"In July 1993, the Municipality initially funded through a community housing development organization (CHDO) the construction of a 121-unit housing project named Estancias del Rio. The agreement with the CHDO indicated that the construction should have been completed in August 1997."

Municipality's Comments

The Municipality disagrees.

The initial agreement for this project was signed on September 16, 1995 for land acquisition, soft and development costs with funds from FY 1993. Funds were disbursed for these purposes on 1997. It was impossible for the project to be constructed by 1997 if that was the year when the first disbursement of HOME funds was made for land acquisition. Such contention is an error in the written agreement.

A chart of all HOME grant agreements for this project is enclosed as supporting documentation. All HOME grant agreements for this project were available for inspection by the auditors.

OID's contention

"Regulations at 24 CFR 92.205(e) provide that a HOME-assisted activity that is terminated before completion, either voluntarily or otherwise, constitutes an ineligible project and any HOME funds invested must be repaid to the participating jurisdiction's treasury account."

Comment 2

Comment 2

Municipality's Comments

Municipality disagrees

This project has not been terminated. It is currently undergoing construction. Seven units have been completed, since the new CHDO reinitiated construction on the project on October 2010. These 7 units are ready for acquisition by eligible homebuyers. Reports show that nearly 100% of the infrastructure of the project is completed.



OIG's contention

"The CHDO responsible for the development of Estancias del Rio defaulted on the construction loan, and in June 2006, the bank foreclosed on the loan. As a result, the construction work stopped."

Municipality's Comments

The Project was not foreclosed by the bank. Citibank declared the loan due and payable and requested full payment. Later on obtained judgment and commenced foreclosure procedures which were never completed.

OIG's contention

"In a letter, dated October 27, 2010, HUD informed the Municipality of its decision, disallowing all funds disbursed, requesting the reimbursement of more than \$4.3 million, and prohibiting any additional funding to the housing project. 1

Comment 3

Comment 4

During the audit, we consulted HUD headquarters about the propriety of using \$400,000 in HOME funds to pay off the defaulted construction loan. In its response, HUD informed us and the San Juan HUD CPD field office that the Estancias del Rio housing development was not compliant with program requirements. As a result of our review and inquiries, HUD requested the reimbursement of all funds.

Municipality's Comments

Comment 4

Which of the statutes or regulations that govern the use of HOME funds has the Municipality violated in regards to the Estancias del Rio project? Who in HUD and in the San Juan CPD field office made such a statement and on which elements did they based such a determination? On what support is such a claim made?

The Municipality is very aware of the elements affecting the appropriate use of HOME funds and has been extremely vigilant to see that every payment disbursed in this project has been on an eligible activity and for an eligible cost. All disbursements on the project have been analyzed and classified as eligible cost and supporting documentation was verified. This information was available for inspection by the auditors.

Documentation that evidences the actions

1. Grant Agreement Table for the Estancias Project
2. Subsidy Layering Analysis (Grant Agreement dated May 27th, 2010)
3. Allocation of HOME funded costs of the original project (Grant Agreement dated May 27th, 2010)
4. Revolving Fund and Cash Flow Estimates (Grant Agreement dated Sept. 17, 2010)
5. Subsidy Layering Analysis – Project Liquidation (Grant Agreement dated Sept. 17, 2010)
6. Assumptions for Subsidy Layering Analysis, Cash Flow and Sales Proceeds (Grant Agreement dated Sept. 17, 2010)
7. CHDO's monthly progress reports for the Months of November, December, January and February

Finding 1B – Put to better use \$906,091

“Require the Municipality to reprogram and put to better use \$906,091 associated with unexpended funds for the Estancias del Rio housing project”

Municipality's Comments

For the reasons discussed in Finding 1A, and the following comments, the Municipality disagrees with this recommendation.

HOME funds allocated to the project are necessary according to the Subsidy Layering Analysis. On May 27th, 2010 a grant agreement was signed with the new CHDO and HOME funds were committed in the amount of \$1,206,541.18. HOME funds were disbursed after the execution of an amendment to grant agreement whereby new CHDO committed to invest the developers fee in the construction of the units. Developer's fee and soft costs amounted to approximately \$300,000. The difference is the \$906,091 that OIG is requesting to put to better use.

The most important reason for the use of these funds is that the project has not stopped the construction of the HOME assisted housing units. In fact 7 units are completed and ready for acquisition by an eligible participating family. Please see the monthly reports submitted by the CHDO for the months of November, December, January and February.

The Municipality is in full compliance with the dispositions of Section 203 of the Cranston-González National Affordable Housing Act, as amended. The stated purpose of this Act is to “expand the supply of decent, safe, sanitary and affordable housing [...] for very low income and low income Americans.”

When completed this project will expand the supply of affordable housing units and made them available to 64 for very low income and low income participants.



The CHDO has already interviewed 147 families of which 86 have been evaluated and 70 were found eligible to participate in the HOME assisted activity. Four families have obtained the approval of the mortgage and are in the process of acquiring housing units from the inventory of completed units in the project.



There is no better use for these funds.



The Cranston-González Act is not violated by proceeding with the construction of this project. Stopping the project and reprogramming these funds would be the conduct in violation of the Act.

Homebuyer Assistance Activity #1141 – this activity was initially funded in July 2007, providing \$10,000 in HOME assistance to a participant for the acquisition of a home. In April 2009, the Municipality withdrew from HUD the full amount, but it had not disbursed any funds toward the acquisition of the home. [...]

Regulations at 24 CFR 92.502(C)(2) state that HOME funds withdrawn from the treasury account must be expended for eligible costs within 15 days.[...]

Recommendation on Homebuyer Activity 1141

The Municipality should not continue with this activity and must reimburse \$10,000 in HOME disbursement.

Municipality's Comments

The Municipality agrees with the recommendation.

Actions in response to the recommendation

On March 3rd, 2011 the Municipality of Mayaguez electronically transferred to the US Treasury Federal Reserve the \$10,000 corresponding to the funds withdrawn for IDIS Activity #1141.

Date of completion of actions in response to recommendation Comments to Finding 1A

Action was completed on March 3rd, 2011

Documentation that evidences the actions on Finding - Homebuyer Activity 1141

See enclosed supporting documentation:

1. Banco Popular Outgoing Transfer of Funds Form PR29861 with the Ref. No. or Test Key 2011030329861218.

Comment 5

2. Municipality's Disbursement Request Form ["Comprobante de Desembolso"] #HOME-077, Dated February 23, 2011 for the amount of \$10,035. The \$35.00 corresponds to the cost charged by the bank for the electronic funds transfer.
3. Municipality's check No. 005194 dated February 25, 2011 for \$10,035.

Finding 1C - Villas de Felisa Housing Project

"The Municipality could not support the income eligibility of the participants as required by HUD.3 Therefore, HUD lacked assurance of the allowability and allocability of more than \$2.4 million charged to the HOME program. [...]

The HOME program supervisor informed us that the eligibility determination function was delegated to the developer of the housing project which made the determination and kept the participant records, and that no independent verification was made. The Municipality could not support the income eligibility of the participants as required by HUD. [...]

The activity remained open in HUD's information system because the Municipality did not have the required information on participants, including information to support that income eligibility requirements had been met."

Recommendation 1C

"Require the Municipality to submit all supporting documentation showing the allowability and allocability of \$1,062,991 disbursed for participant families at the Villas de Felisa housing project or reimburse this amount to its HOME treasury account or HUD, as appropriate, from non-Federal funds."

Comment 6

Municipality's Comments

Municipality disagrees with Finding 1C.

The Municipality did take the appropriate measures to ensure that subsidized units were occupied by eligible participants. The HOME program supervisor incorrectly informed that eligibility determination was performed by the developer based on information provided by staff who worked on the program at the time. The eligibility determination was performed by the Municipality's HOME program personnel. OIG Auditors were informed before the exit conference that participant's records were available at the Municipality's facilities for inspection.

Comment 6

The Municipality has indeed entered into HUD's Information System the required information of 115 participants who received HOME subsidy.

Home funds disbursed for this project add to \$2,416,000.00

Comment 6

The information of each participating family shows the following:

The aggregated amount of subsidy allocated to participating families is \$2,074,283.42

Therefore, there is a difference of \$341,716.58

The Municipality is requesting that the difference of \$341,716.58 be considered as a development subsidy. This allocation is permitted by the HOME regulation *24 CFR 92.206*.

The development subsidy allowed the developer to offer the housing units at a lower sale price to families of low and very low income making it possible for them to acquire housing units in the project.

Actions in response to the recommendation

The Municipality entered in HUD's Information System the required information of 115 participants who received HOME subsidy.

The Municipality is formally requesting HUD to approve that the funds not allocated to participating families be considered as development subsidy as permitted by HOME regulation *24 CFR 92.206*. The Activity will be closed subject to HUD's approval of the allocation of the difference between the total HOME funds disbursed to the project and the \$341,716.58, not allocated to participating families to be considered as development subsidy. See supporting documentation for actions taken in response to Finding 2A.

Comment 6

The Municipality is enclosing 30 digitalized records of participating families with income eligibility determinations handwritten by the HOME Program technicians. The size of the sample equals 26% of the total participating families.

Estimated Date of completion of actions in response to recommendation

The Activity will be closed subject to HUD's approval that the difference in the amount of \$341,716.58, not allocated to participating families be considered development subsidy.

Documentation that evidences the actions on Finding 1C

Please refer to the following supporting documents:

1. Digitalized records of 30 participating families.
2. HUD's Information System Report – HOME Multi-Address Activity Summary, Homebuyer

Questioned costs

The total amount of questioned costs in this finding is \$1,062,991

Management's projection of cost savings from implementation of recommended actions - \$341,716.58

Comment 7

Finding 1D - Villas de Felisa Housing Project

Recommendation 1D

Require the Municipality to reimburse its HOME treasury account or HUD, as appropriate, from non-Federal funds \$273,009 paid for land that did not provide the intended benefits.

Municipality's Comments

The Municipality disagrees.

The Municipality used or developed 22.8951 "cuerdas" from the 24.5717 "cuerdas" of land acquired for Villas de Felisa Housing Project.

According to the Plans and Resolutions approved by the "Administración de Reglamentos y Permisos de Puerto Rico" [ARPE], under Act 135 of July 15, 1967, as amended, and Regulation 12, after the housing units were completed the segregation of each parcel was approved. The Resolutions also identified that after a survey, the land acquired measures 24.5717 "cuerdas".

Plans and Resolutions approved by ARPE, included as supporting documents, evidence that the only Parcel approved for future construction of housing units is Parcel VII which measures 1.6766 "cuerdas". The remaining land is dedicated to public uses like condominiums, green areas, streets, etc. and may not be used for the construction of more housing units.

The amount paid for land from HOME funds was \$916,000.00 and \$120,000.00 from CDBG for a total amount of \$1,036,000.

Comment 7

Based on the total purchase price for 24.5717 "cuerdas" of land acquired, the parcel segregated for future use, identified as Parcel VII, which measures 1.6766 "cuerdas" equivalent to 6589.6280 sq. mt., the value of Parcel VII is \$70,689.36.

The developer has not complied with the Deed of Conditional Assignment of Real Estate for Joint Venture executed with the Municipality and the HOME Agreement whereby it is obliged to revert Parcel VII of 1.6766 "cuerdas", segregated for future development to the Municipality, free of liens and encumbrances. The developer has to revert the title of Parcel VII to the Municipality before the Municipality is able to dedicate this land to the construction of housing units.

Comment 7

Action to be taken

The Municipality will pursue legal action against the developer.

Once title of Parcel VII is transferred to the Municipality, a Request for Proposal will be published for the construction of affordable housing units in compliance with HUD's regulations 24 CFR92. 205 (a)(2).

Estimated Date of completion of actions in response to recommendation

One year to execute agreement with developer or contractor once the Request for Proposal has been published for the construction of affordable housing units in compliance with HUD's regulations 24 CFR92. 205 (a)(2) and the entity to carry out the project is selected.

Documentation that evidences the actions on Finding 1D

Present condition

1. A digitalized copy of the Plans and Resolutions approved by ARPE

Documents that will evidence final action on Finding 1D

1. Deed of Transfer of Parcel VII to the Municipality
2. Request for Proposal
3. Agreement with developer or contractor

Questioned costs - \$70,689.36

The total amount of questioned costs in this finding is \$273,000. This is based on an incorrect assumption of the size and value of the land available for future development in compliance with HUD's regulations 24 CFR92. 205 (a)(2).

The correct value of the land available for future development is \$70,689.36.

Finding 1E – Monitoring Procedures

Recommendation 1E

"Require the Municipality to establish and implement appropriate monitoring procedures to ensure HOME requirements and objectives are met."

Comment 8

Municipality's Comments

The Municipality agrees.

The Municipality does have and implements a Monitoring Procedures Manual that is described in the Consolidated/Action Plan 201, 2011 to 2014 and the Monitoring Unit Director has developed a Monitoring Work Plan for Fiscal Year 2010-2011.

Nevertheless, the Municipality agrees with the OIG contention that monitoring procedures must improve.

Actions in response to the recommendation

A comprehensive Preliminary Financial Management System is being developed based on HUD's Training Manuals for financial management, the technical assistance from the Municipality's IDIS and legal consultants, and HUD's pertinent personnel.

Monitoring Unit Personnel, specially qualified in accounting and monitoring reviews, has been designated to carry out the oversight activities described in the Financial Management System Procedures Manual and report to the Monitoring Unit Director and the Municipality's Housing Department's Manager.

Date of completion of actions in response to recommendation

March 2nd, 2011 - The Preliminary Financial Management System

On a continuous basis - the oversight activities will be carried out by the Monitoring Unit Personnel.

Monthly reports will be produced.

Documentation that evidences the actions corresponding to Finding 1E

Please refer to the following documents as they are the supporting documentation for Findings 1E, 2F and 2H of this Audit's draft.

1. Preliminary Financial Management System
2. Monitoring Unit Employees' Job Description
3. Monitoring Unit Employee Resumé

Questioned costs - None

Comment 9

Finding 2: **The Municipality's Financial Management System Did Not Comply With HUD Requirements**

Finding 2 A - Unsupported Program Disbursement

"The Municipality did not provide documentation supporting the reasonableness, allowability, and allocation of \$1.5 million charged to the HOME program, associated with the Villas de Felisa housing project. It paid for construction work without progress/engineering certifications, cost descriptions, or other support showing the work or service that was performed."

Recommendation 2A

"Require the Municipality to submit all supporting documentation showing the eligibility and propriety of \$1.5 million charged to the HOME program for the development of the Villas de Felisa housing project or reimburse the program from non-Federal funds."

Municipality's Comments

The Municipality disagrees and requests the finding be removed from audit's draft as it is submitting supporting documentation that shows the eligibility and propriety of \$1.5 million charged to the HOME program for the development of the Villas de Felisa housing project.

The Municipality in compliance with Regulation 24 CFR 92.205(a) allowed disbursements for an eligible activity which included new construction, real property acquisition, site improvement, and other expenses including financing costs.

Furthermore, in compliance with HUD's record keeping requirements of 24 CFR 508(A)(3)(ii) and 24 CFR 85.20, the Municipality had available for audit documentation supporting the reasonableness allowability and allocation of \$1.5 Million charged to the HOME program, associated with the Villas de Felisa Housing Project.

For example, the Municipality had appointed Eng. Israel Alvarez, as the engineer in charge of overseeing construction works in process and submitting progress status report. During the construction of the project, Eng. Venegas was appointed Housing Director for the Municipality. Eng. Venegas was also in charge of overseeing construction works in process and submitted progress status report. These documents were available for inspection during the audit.

The Municipality evaluated proposals from different developers before making the final selection. The selected proposal clearly identified the need for HOME funds. It included as equity land acquisition and distributed HOME funds with owner's investment in different items of soft and hard construction costs.

The Municipality approved the submitted project's budget and later approved amendments for construction items not included in the developer's costs breakdown and FHA Form 238 – "Contractor's and Mortgage Breakdowns" – contractor's and mortgage breakdowns included in the proposal.

The Municipality also requested a Payment Bond and a Rider which clearly identified the amount of the construction contract for \$10,250,000 million a similar amount as the one considered in the estimated construction and loan projections submitted to Citibank.

During construction works the Municipality requested copy of weekly payrolls from the general contractor and subcontractor. This documentation clearly established that construction was undergoing.

Legislation creating the HOME Partnership Program was enacted on 1992. Soon after, in 1996 the Municipality began the process of identification of real property acquired for the construction and development of the Villas de Felisa Housing Project. This was the Municipality's first experience developing a housing project under the HOME Partnership Program statutes and regulations.

The Municipality relied in the summary of terms of the construction loan between Citibank and developer which included a cash flow with an estimated construction breakdown.

The Municipality relied in the above mentioned documentation to disburse HOME funds.

In addition to this, the Municipality has performed a subsidy layering analysis which supports that \$1.5 million disbursed for new construction, in addition to funds disbursed for land acquisition, were needed in order to provide affordable housing units for low and very low income families.

According to the Municipality's records, which include settlement statements, the families qualified for a mortgage loan in an average of \$54,900. The gap between the mortgage and selling price was covered with HOME funds disbursed for construction.

Assumptions for the subsidy analysis include units for low and very low income families according to a preliminary estimate of the available market. According to these projections the project required \$2,839,600 in subsidies in order to be affordable for low and very low income families. Subsidy analysis and assumptions are included.

Actions in response to the recommendation

The Municipality is hereby submitting supporting documentation that shows compliance with regulation 24 CFR 92.2059(a) which allows disbursements for reasonable expenditures associated with the HOME program and regulations 24 CFR 92.508(a)(3)(ii) and 24 CFR 85.20 record keeping requirements.

Date of completion of actions in response to recommendation

No action required.

Documentation that evidences the actions corresponding to Finding 2A

Documents provided by the developer and approved by the Municipality are hereby included as supporting documentation which demonstrates compliance with the record keeping requirements of 24 CFR 92.508(a)(3)(ii) and 24 CFR 85.20 and 24 CFR 92.205(a) which allows disbursements for reasonable expenditures associated with the HOME program.

1. Developer's Cost Breakdown included in proposal dated October 3rd, 1996
2. FHA Form 2328 – Contractors and Mortgages Breakdown included in proposal dated October 3rd, 1996
3. Letter dated October 26, 1998 (Adjudication of Construction Contract to SLG for \$10,250,000.00)
4. Performance Bond, Surety Rider (\$10,250,000.00)
5. Citibank Commercial Banking Group – Summary of Terms - Cash Flow (January 1998)
6. Copies of Weekly Payroll from SLG (General Contractor)
7. Copies of Weekly Payroll from Electrical Sub-Contractor
8. Progress Reports (% completion) – March 12, 1999; April 5, 1999; May 25, 1999; June 4, 1999; Sept. 18, 2002; Sept. 23, 2002
9. Letter dated June 7, 1999 – authorization of developer to General Contractor for the carriage of unused material
10. Carriage of unused material (Invoice and Charts, June 15, 1999; June 21, 1999)
11. Subsidy analysis for Villas de Felisa project
12. Assumptions for subsidy analysis for Villas de Felisa Project

Questioned costs - \$1,500,000

Finding 2 B - Ineligible Program Disbursements

“The Municipality allowed the disbursement of more than \$130,000 in HOME funds for 28 solar powered street lights that did not provide the intended benefits. The consolidated annual performance and evaluation report for fiscal year 2008-2009 reported that the illumination at the Estancias del Rio housing project was provided with solar powered street lights. On July 15, 2010, we visited the housing project facilities and found that there were no solar powered street lights.

Comment 10

Regulations at 2 CFR Part 225 (appendix A, C.3.) provide that a cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.

Municipality's response

The Municipality disagrees and requests finding 2B be removed from audit's draft.

The 28 solar powered street lights did indeed provide the intended benefits. They were installed following commitments made by the U.S. Department of Housing and Urban Development to promote energy efficiency in HUD's inventory of public and assisted housing, as well as in housing financed through its formula and competitive grant programs.

Relative benefit analysis must be applied in light of a series of Congressional Actions impacting HUD at that period of time. The historical background for the Municipality's determination to install the solar powered street lamps is as follows.

A Department of Energy Task Force was tasked in 2002 to respond to the challenge of rising energy costs to residents and owners of HUD-assisted properties. The Task force identified a series of actions that HUD could undertake to address the need for energy conservation and energy efficiency in HUD's own programs.

Section 154 of the Energy Policy Act of 2005 ordered the Secretary for Housing and Urban Development to "develop and implement an integrated strategy to reduce utility expenses through cost-effective energy conservation and efficiency measures and energy-efficient design and construction of public and assisted housing. The energy strategy shall include the development of energy reduction goals and incentives for public housing agencies."

In August 2006, as directed by Congress, pursuant to Section 154 of the Energy Policy Act of 2005, HUD submitted its energy strategy for HUD's inventory of public and assisted housing in the publication entitled "Promoting Energy Efficiency at a Time of Change"

This document included a list of HUD's Energy Strategy - Planned Actions later known as HUD's Energy Action Plan.

Items No. 6 of the planned actions listed in this document specifically concerns the area of Community Planning and Development. The document reads as follows:

"6. Encourage energy efficiency in HOME and CDBG-funded new construction and housing rehabilitation projects."

Congress had directly instructed the Secretary for HUD to implement energy efficient and green building practices. In accordance with this directive, the Municipality voluntarily incorporated energy efficient elements in the Estancias del Rio project. Installed elements were the standard technology at that moment of their incorporation to the project.

Comment 10

The selection and installation of this equipment was made in consultation with the local officials of the Department of Energy. This Agency provided counsel in selecting the equipment that complied with all applicable technical specifications.

At the time of their installation, the solar powered street lights worked according to specifications. Performance was consistent with specifications for a period of time that exceeded 2.5 years. At which moment the technology began to underperform. The amount of light (footprint) became smaller and smaller until some stopped working altogether.

The new technology that was being subsidized in order to promote its development while reducing the energy costs for residents and owners of HUD assisted projects underperformed. As HUD's publication clearly expressed, it was HUD promoting energy efficiency at a time of change. The technology was changing.

By that time the equipment started to underperform, the first phase of the project had been completed and 20 families were living in it.

The families already living in the project needed the street lamps in full working order for their safety. They approached Municipal Officials requesting the replacement of the solar powered street lighting system. The stated reason for this request was that they feared for their safety.

At that moment, the Municipality reviewed the state of the solar powered street lamp technology and determined there were no alternatives that would ensure solar street lamps would work indefinitely.

So, in order to provide for the safety of the residents and compliance with the requirements of HUD's Housing Quality Standards of providing "decent, safe, and sanitary units" replaced with non-federal funds the non-working street lights with traditional ones.

Comment 10

Nevertheless, the installed solar powered street lights did provide the service that was intended up to the extent the technology of the time allowed. Relative benefit analysis must be applied in light of the performance of similar technology installed around the same time pursuant to the Congressional Actions impacting HUD.

When analyzing this matter it must be taken into consideration that the solar power technology available at that moment was not as advanced as today. The solar powered street lamps worked as the technology permitted at that moment.

Any relative benefit analysis must be applied in light of the circumstances in which these costs were incurred. The Municipality acted following the Congressional directive to subsidize the implementation of energy efficient technology. The fact that the technology did not perform indefinitely must not be used to penalize a Municipality that, after all, was acting in good faith by voluntarily complying with Congressional directives to HUD and in accordance with HUD's Energy Action Plan.

Documentation that evidences the actions corresponding to Finding 2B

Enclosed documents:

1. Energy Desk Book for HUD Programs
2. Energy Task Force – Implementing HUD’s Energy Strategy
Submitted Pursuant to Section 154
Energy Policy Act of 2005
3. HUD’s Energy Action Plan
 - a. Page 13 of the Energy Task Force Document

Questioned costs - \$130,000

Finding 2C Inaccurate Accounting Records

“The Municipality’s accounting records were not accurate, current, and complete. They did not reflect complete financial information on HOME activities and did not permit the adequate tracing of program expenditures. For example, the expenditures shown in the Municipality’s accounting records did not agree with amounts reflected in HUD’s information system.

Regulations at 24 CFR 85.20(a) require participating jurisdictions to maintain fiscal controls and accounting procedures sufficient to permit the preparation of reports and the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes.

The Municipality could not explain the discrepancies and could not account for more than \$23,000 drawn from HUD for various HOME activities.

Activity Type	HUD’s Information System	Accounting Records	Differences
Estancias Del Rio	\$4,096,677	\$4,085,015	\$(11,662)
Home-buyer assistance (as of April 30, 2010)	\$387,402	\$376,000	(11,402)
Tenant-based rental assistance (as of June 30, 2008)	\$82,715	\$81,917	(798)
Total			\$(23,862)

Municipality’s Comments

Municipality disagrees in part and agrees in part. Corrective actions have been completed. Finding should be cleaned and not included in the publication of the Audit’s Final Report.

Comment 11

Actions in response to the recommendation

The Municipality is hereby accounting for the discrepancy and explaining the corrective actions undertaken.

Finding on the Estancias del Rio activity

The amount of \$11,662 that appears as a difference between HUD's Information Systems and the Accounting Records is incorrect. The correct amount is \$11,668. This difference is due to the fact that more funds than necessary were requested for the CHDO's administrative expenses. Once downloaded, these funds were never disbursed.

Action taken – In this case HOME funds were drawn but never disbursed. Therefore, the Municipality has followed the recommendations made by OIG officials on how to proceed with the funds questioned on the finding pertaining to Homebuyer Assistance Activity #1141, were HOME funds were drawn but not spent. The Municipality has reimbursed the amount in question to the US Treasury Federal Reserve.

Date of completion of action in response to recommendation March 3rd, 2011

Documentation that evidences the actions corresponding to Finding 2C – Estancias del Rio activity

See enclosed supporting documentation:

- a. Banco Popular Outgoing Transfer of Funds Form PR29861 with the Ref. No. or Test Key 2011030329861218.
- b. Municipality's Disbursement Request Form ["Comprobante de Desembolso"] #HOME-078, Dated March 3rd, 2011 for the amount of \$11,703. The \$35.00 difference corresponds to the cost charged by the bank for the electronic funds transfer.
- c. Municipality's check No. 005198 dated March 3rd, 2011 for \$11,703.
- d. Memorandum dated May 20th, 1999 addressed to Mr. Nelson Vélez Seda, then Director of the Municipality's Department of Housing and Federal Programs, from Mr. Joseph Valentín Rivera, then IDIS technician, informing that "they had exceeded the amount of funds requested for the CHDO's administrative expenses in the amount of \$11,668."

Questioned costs – \$11,662

Finding on the Homebuyer Assistance activity (as of April 30, 2010)

The amount of \$387,402 that appears in the OIG's review as the amount that appears in the HUD Information system is incorrect. As discussed between Mr. Eddie Morales, HOME Program Personnel in charge of the Accounting Books and Mr. Germán Pérez, Senior Auditor. The correct amount is \$341,000. The explanation is as follows:

Comment 12

The discrepancy originates at the moment reports comparing funds requested with funds disbursed, included activities not pertaining to Homebuyer, but pertaining to New Construction which were incorrectly included in this report because of an involuntary mistake.

Therefore, the amount that appears as assigned to Homebuyer in HUD's Information System was artificially increased to \$387,402 with the funds from the New Construction activity. Once the funds from the Homebuyer activity are removed, the total amount requested and the total amount disbursed on the Homebuyer activity coincide in both the Accounting Records and HUD's Information System. The amount that appears in both is \$341,000.

- a. The IDIS Homebuyer Disbursement Report of 2009 indicates a total amount disbursed in this activity of \$341,000.
- b. In the Municipality's Accounting Records the total amount paid according to the HOME Program Breakdown Disbursement Report is \$376,000
- c. Minus cancelled check No. 004494 in the case of Norberto Forestier Soler \$35,000
Total amount requested as per the Accounting Records \$341,000

Actions in response to the recommendation

The discrepancy claimed in this finding has been clarified by the Municipality and therefore the finding must not be included in the publication of the Audit's Final Report.

Documentation that evidences the actions corresponding to Finding 2C –Homebuyer Activity

See the enclosed supporting documents

- 1) HOME Program Breakdown Disbursement by Activity Report
- 2) IDIS Homebuyer Report for 2009
- 3) A copy of Check No. 004494 for the amount of \$35,000 to Mr. Norberto Forestier Soler

Questioned costs - \$11,402

Comment 13

Finding on the Tenant Based Rental Assistance activity (as of June 30th, 2008)

The Accounting Records of the Drawdown Reports indicate	
a total disbursement of	\$81,917.19
Revising each amount disbursed, it was found that by mistake two disbursements pertaining to administrative travel expenses were included	<u>\$94.60</u>
Sub-Total	\$81,822.59

Comment 13

Plus a payment for rental assistance that was not reported on the Accounting Records,	<u>\$895.49</u>
Total	\$82,718.08
Amount not requested from the US Treasury	\$2.94

The amount not requested from the US Treasury was covered with the interests accumulated in the HOME Program Bank Account as permitted by the regulation.

Actions in response to the recommendation –

The discrepancy claimed in this finding has been clarified by the Municipality and therefore the finding must not be included in the publication of the Audit's Final Report.

Documentation that evidences the actions corresponding to Finding 2C –Tenant Based Rental Activity

See the enclosed supporting documents:

- a) HOME Program Breakdown Disbursement Report for Program Year 2008
- b) Travel expense payment's by checks #004136 and #004137
- c) Check #004225 for rental payment of \$895.49
- d) IDIS TBRA report for program year 2008

Comment 14

Finding 2D Deobligate \$2,008

Recommendation 2D

"Require the Municipality to deobligate in HUD's information system, then reprogram and put to better use, \$2,008 associated with unexpended funds related to the completed activities."

Municipality's response:

Municipality agrees. Funds have been deobligated. This finding must be removed from Audit's draft.

Actions in response to the recommendation

The Municipality has deobligated \$2,008 corresponding to IDIS activities 869, 858 and 873.

Date of completion of actions in response to recommendation March 5th, 2011.

Documentation that evidences the actions corresponding to Finding 2D

1. HUD Information System Report- Printed screen of IDIS status page indicating activity is closed.

Questioned costs - \$2,008

Comment 15

Finding 2-E HOME Funds not Disbursed in a Timely Manner

Recommendation 2-E

“Require the Municipality to establish and implement adequate procedures to ensure that it disburses HOME funds for eligible activities within HUD’s established timeframes.”

Municipality’s Comments

Municipality agrees and explains.

At the Program level, the Municipality already has established specific measures to assure that HUD HOME Program disbursements in eligible activities, comply with HUD timeframes (Grants Management requirements). Those measures and procedures are included as part of the designed, Preliminary Financial Management System enclosed as supporting document for Findings 1E, 2F and 2H of this audit draft.

It is the Municipality’s Department of Housing and Federal Programs the entity that administers the HOME Partnerships Program. This Department does not control the entire payment process and the disbursement of HOME funds. It is the Municipality’s Finance Department, the entity that has the ultimate responsibility for issuing payments and the disbursement of HUD HOME funds.

Comment 15

Actions in response to the recommendation

On March, 2, 2011 the Manager for the Municipality’s Housing and Federal Programs Department sent a letter to Municipal Finance Department Manager requesting a meeting with the Municipal Finance Department Manager and all the personnel of the above mentioned Department that works in the payment and funds disbursement process, in order to take steps and implement all necessary policies to correct this situation and comply with HUD HOME Program Grants Management requirements.

Date of completion of actions in response to recommendation

We expect with the collaboration of the Municipal finance Department, to establish all the necessary procedures and policies in the next one hundred twenty (120) days.

Documentation that evidences the actions on Finding 2E

Letter dated March 2nd, 2011 addressed to Mr. Luis Olivares, Manager of the Municipality’s Finance Department.

Questioned costs – None

Comment 16

Finding 2F – Inaccurate Reporting

Recommendation 2F

“Require the Municipality to establish and implement adequate controls and procedures to ensure that accurate commitment and activity information is reported in HUD’s information system.”

Municipality’s response

Municipality agrees.

Actions in response to the recommendation

The Municipality has already established a Preliminary Financial Management System to ensure each HOME funded activity that is entered into IDIS is reviewed in order to correct any inaccurate information, including funding amount, activity status and funding type classification, as recommended by the OIG Auditors.

That Financial Management System involves personnel of the Department of Housing and Federal Programs Monitoring Unit, the HOME Program Coordinator and technicians, the CPD Fiscal Unit personnel, including the IDIS Official, the HOME Program Legal Advisor and HUD’s technical assistance personnel at the San Juan Field Office.

Date of completion of actions in response to recommendation

We expect to complete the revision process in the next one hundred twenty (120) days.

Documentation that evidences the actions corresponding to Finding 2F

Please refer to the following documents as they are the supporting documentation for Findings 1E, 2F and 2H of this Audit’s draft.

1. Preliminary Financial Management System
2. Monitoring Unit Employee Job Description
3. Monitoring Unit Employee Resumé

Questioned costs – None

Comment 17

Recommendation 2G – Municipality must review all grant agreements

“Require the Municipality to review all grant agreements for each activity entered into HUD’s information system and correct any inaccurate information, including funding amount, activity status, and funding type classification.”

Municipality’s response

The Municipality agrees.

Actions in response to the recommendation

The HOME Partnerships Program’s legal advisor has already been instructed to revise all grant agreements and make all necessary recommendations to correct any inaccurate information, including funding amount, activity status, and funding type classification.

Date of completion of actions in response to recommendation

Agreements should be revised and corrections made in no later than 120 days.

Documentation that evidences the actions corresponding to Finding 2G

1. Letter dated March 3rd, 2011 addressed to Ms. Luz C. Toro, Esq., legal counsel for the
2. Municipality’s HOME Partnership Program requesting the revision of all of the program’s grant agreements.

Questioned costs – NONE

Comment 18

Finding 2H – Lack of Procedures and Controls

Recommendation 2H

“Require the Municipality to develop and implement a financial management system that permits the tracing of HOME funds to a level which ensures that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes and that funds are drawn and used for their intended purpose only.”

Municipality’s response

Municipality agrees.

Actions in response to the recommendation

As recommended by the OIG Auditors, the Municipality has already developed and designed a Preliminary Financial Management System. That Preliminary Financial Management System will

allow the Department of Housing and Federal Programs administrators, to trace HOME funds to a level that ensure such funds will not been used in violation of the restrictions and prohibitions of applicable statutes and that funds are drawn and used for their intended purpose only.

The implementation of the Financial Management System involves the active participation of the Department of Housing and Federal Programs Monitoring Unit personnel. The Monitoring Unit personnel is responsible for the Monitoring Process and Oversight of all HOME Program funded activities and projects.

The Monitoring Unit, as part of the HUD Consolidated Action Plan developed an Annual Monitoring Plan. That Plan includes Monitoring Interventions to all HOME funded activities and projects, including CHDO Projects.

Date of completion of actions in response to recommendation

We expect to fully implement the Preliminary Financial Management System, in the next sixty (60) days.

Documentation that evidences the actions corresponding to Finding 2H

Please refer to the following documents as they are the supporting documentation for Findings 1E, 2F and 2H of this Audit's draft.

1. Preliminary Financial Management System
2. Monitoring Unit Employee Job Description
3. Monitoring Unit Employee Resumé
4. Monitoring Plan for FY2010-1011

OIG Evaluation of Auditee Comments

Comment 1 The Municipality believed that it complied with all program requirements. It stated that the Cranston Gonzalez Act and HUD regulations did not establish timeframes for the completion of HOME assisted activities. The Municipality also stated that it submitted a request for reconsideration of HUD's ineligibility determination of the Estancias Del Rio housing project. Furthermore it stated that a write-off of \$3.4 million of the HOME funds disbursed was needed to make the project feasible and reduce the sales price of the housing units to market value.

We agree with HUD's determination that the Estancias Del Rio housing project was inconsistent with HOME regulations, and therefore the activity was ineligible. While the Cranston Gonzalez Act does not specifically set time limits for the expenditure of HOME funds, HUD regulations at 24 CFR 95.500(d) provides specific timeframes for such expenditures. The Municipality had not been able to complete this housing project in more than 17 years since its initial funding date. Therefore, it is not consistent with HOME objectives. We are concerned with the viability of this activity since the Municipality proposes the write-off of HOME funds to make the project feasible and reduce the sales price of the housing units to market value. The Municipality did not provide adequate support that could substantiate their position. Accordingly, we did not modify the report finding and recommendations.

Comment 2 The Municipality contends that the Estancias del Rio project has not been terminated and regulations at 24 CFR 92.205(e) are therefore not applicable.

In its letter dated October 27, 2010, HUD informed the Mayor of the Municipality of Mayaguez of its management decision to disallow all funds previously invested in the Estancias del Rio project and prohibited any future investments in the project. The letter instructed the Municipality to repay all HOME funds invested, or agree to a voluntary grant reduction. The project has therefore been effectively terminated by HUD. In addition, the Municipality recognizes that to make this project feasible it will require a write off of more than \$3.4 million in HOME funds previously invested. As a result, we do not agree with the Municipality's comments.

Comment 3 The Municipality informed that the Estancias del Rio project was not foreclosed by the bank.

On August 31, 2007 the court entered a judgment in favor of Citibank for more than \$1.8 million. With this decision the bank could have commenced foreclosure procedures on the mortgage note with the developer. For this reason, the Municipality used more than \$400,000 in HOME funds to pay off the defaulted construction loan and avoid foreclosure. Nevertheless, we clarified the situation and removed the statement from the report.

Comment 4 The Municipality contends that no statutes were violated when it used \$400,000 in HOME funds to pay off the Estancias del Rio project defaulted construction loan.

Under regulations at 2 CFR 225 Appendix B. Item 16, funds used for settlements resulting from violation or failure of the governmental unit to comply with federal or local laws are unallowable. During the audit we consulted with HUD on the propriety of using \$400,000 to pay off the defaulted construction loan. As a result, HUD determined that all funds invested in the project are disallowed. The Municipality will need to work with HUD during the audit resolution process to demonstrate the propriety of using \$400,000 to purchase the outstanding construction loan as well as the propriety of other funds invested in the project.

Comment 5 The Municipality stated it reimbursed the \$10,000 withdrawn for activity #1141. However, the Municipality did not provide additional documentation that could demonstrate it cancelled the activity and reprogrammed the funds to other eligible efforts. It will need to provide documentation to HUD to show that the funds were properly reprogrammed.

Comment 6 The Municipality stated that it took appropriate measures to ensure that Villas de Felisa subsidized units were occupied by eligible participants. It stated that the HOME program supervisor incorrectly informed us that the eligibility determination was performed by the developer; it was done by HOME program personnel and provided electronic copies of 30 participant files.

We eliminated this statement from the report. Also, the Municipality indicated that it had entered into HUD's information system the required information of 115 participants who received the HOME subsidies. The Municipality stated that of the \$2.416 million in HOME funds disbursed, only \$2.074 million were used on subsidies to participants, and requested that the difference of \$341,716 not provided in direct assistance to participants be considered as a development subsidy pursuant to 24 CFR 92.206.

The Municipality did not provide a list of all 115 participants that received HOME subsidies and the amount of assistance provided to each participant. The information provided was in summary form and could not be appropriately evaluated. HUD will need to review detailed information in order to ascertain that the data has been properly entered in HUD's information system. In addition, according to the supporting documentation the Municipality provided during the audit, the HOME subsidy was for 272 participants/units, but the Municipality now states that subsidies were provided to 115 participants/units. The Municipality did not explain the discrepancy and whether HUD approved such reduction in scope.

We examined two of the 30 case files provided and found deficiencies with the qualification of participants. In one case, the qualifying information appeared to be more than 6 months old at the time of loan closing, and file information was missing. In another case, the income of the participant was above the HOME

program income limits and absent of an explanation of how the income determination was made. Based on the deficiencies found, there is no assurance subsidized units were occupied by income eligible participants. A complete examination of the income eligibility of participants could not be performed because a review of the original documentation is necessary to properly assess the evidence in each file. The Municipality did not provide us adequate support that could demonstrate that all units were occupied by eligible participants. We therefore did not modify the finding and recommendation.

Finally, HOME program regulations at 24 CFR 92.206 do not include provisions for granting development subsidies as an eligible expense for the HOME program. The Municipality did not provide us adequate support that could justify their actions for not providing \$341,716 in HOME subsidy to participants. It will need to provide documentation to establish the allowability and feasibility of this action for HUD's evaluation.

Comment 7 The Municipality believes that the disallowed amount for land acquired for the Villas de Felisa housing project was incorrectly determined and that it should be required to reimburse only \$70,689.

The disallowed amount was determined based on the acquisition price of \$1.036 million for 24.59 acres of land, and not 23.862 acres, (or 24.5717 "cuerdas"), as stated by the Municipality in its comments. According to the documentation provided, approximately 6.48 acres of land had remained unused since being acquired in 1998. This is the land that has remained with the developer and not the 1.628 acres, (1.6766 "cuerdas"), as stated by the Municipality in its comments. The documentation also showed that the Municipality planned to utilize the unused land for the construction and widening of streets, which is not an eligible activity under the HOME program. The Municipality did not provide us adequate support that could substantiate their position. Accordingly, we did not modify the finding and recommendation.

Comment 8 The Municipality stated that it agreed with the recommendation and that the monitoring procedures will be improved. However, the Municipality did not provide us additional documentation that could demonstrate the monitoring procedures in place and that they were in compliance with HUD requirements. It will need to provide documentation to HUD to show the establishment and implementation of monitoring procedures.

Comment 9 The Municipality stated that the \$1.5 million in questioned costs for the development of the Villas de Felisa housing project were properly supported and that the finding should be removed from the report.

The supporting documentation did not provide details showing the work or services paid with each disbursement. The Municipality did not provide us

adequate support that could substantiate their position. Accordingly, we did not modify the report.

Comment 10 The Municipality stated that the finding should be removed because the solar powered street lights worked for a period that exceeded 2.5 years.

The solar powered street lights did not provide the intended benefits and were replaced by regular lights. However, we removed the disallowance and related recommendation because these funds are part of the total Estancias del Rio housing project costs disallowed by HUD in its October 27, 2010, letter to the Municipality.

Comment 11 The Municipality stated that it reimbursed \$11,668 in excessive drawdowns for Estancias Del Rio housing project. However, the Municipality did not provide us additional documentation that could demonstrate it reprogrammed the funds to other eligible efforts. It will need to provide documentation to HUD to show that the funds were properly reprogrammed.

Comment 12 The Municipality stated that the amount shown in HUD's system for its home-buyers assistance activities was incorrect because of a misclassification of a withdrawal. Also, the Municipality indicated that the discrepancy was clarified and the finding should be removed from the report.

The supporting documentation the Municipality provided during the audit did not explain the discrepancy and did not account for \$11,402 drawn from HUD. Despite the misclassification, there is still a difference between HUD's system and the accounting records. The Municipality did not provide us adequate support that could properly explain the discrepancy, show that HUD's information system was accurate, and accounted for the \$11,402 drawn. We therefore did not modify the report finding and recommendation.

Comment 13 The Municipality stated that the discrepancy was the result of a misclassification of two administrative expenditures recorded as tenant-based assistance costs, and a disbursement that was not recorded in the accounting records. Also, the Municipality indicated that the discrepancy was clarified and the finding should be removed from the report.

Although the Municipality explained that it was a misclassification of accounting transactions, it did not provide us additional documentation showing the adjusting entries made in the accounting records reflecting the correct balances of all the accounts involved. It will need to provide documentation to show that the accounting records were properly adjusted.

Comment 14 The Municipality stated that it deobligated the \$2,008 of the completed activities. However, the Municipality did not provide us additional documentation that could

demonstrate it reprogrammed the funds to other eligible efforts. It will need to provide documentation to show that the funds were properly reprogrammed.

Comment 15 The Municipality stated that it agreed with the recommendation and that it initiated corrective measure to ensure it disburses funds for eligible activities and within established timeframes. We acknowledge the Municipality's efforts to address the issues of the finding.

Comment 16 The Municipality stated that it agreed with the recommendation and that it took corrective measure to ensure that accurate commitment and activity information is reported in HUD's system.

Comment 17 The Municipality stated that it agreed with the recommendation and that it initiated corrective measures to review each activity entered into HUD's information system to correct any inaccurate information.

Comment 18 The Municipality stated that it agreed with the recommendation. Also, the Municipality indicated that it had established a preliminary financial management system and provided a handbook with the system to be implemented.

We commend the Municipality for its efforts in addressing the issues of this finding. However, the handbook fails to establish basic accounting controls necessary to maintain an adequate financial management system. For example, it does not require maintaining general ledgers by fiscal year. Also, the responsibility for the financial management system is placed on the monitoring unit personnel instead of the financial management personnel. In addition, procedures established in the handbook are targeted towards monitoring efforts that are unrelated to the financial management function. The Municipality needs to ensure that it establishes a financial system that is in compliance with HUD requirements.