OFFICE OF AUDIT
REGION 1
BOSTON

The Lawrence Housing Authority, Lawrence, MA, Did Not Obtain HUD Approval To Fund a Trust Account And Had Weaknesses in Its Controls

2012-BO-1004 **July 31, 2012**

Issue Date: July 31, 2012

Audit Report Number: 2012-BO-1004

TO: Marilyn O'Sullivan, Director, Office of Public Housing, 1APH

for

FROM: Edgar Moore, Regional Inspector General for Audit, Boston Region, 1AGA

SUBJECT: The Lawrence Housing Authority, Lawrence, MA, Did Not Obtain HUD Approval to Fund a Trust Account and Had Weaknesses in Its Controls

Enclosed is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG's), final audit report on our review of the Lawrence Housing Authority, Lawrence, MA.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation in the body of the report without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8L, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at http://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at 212-264-4174.

July 31, 2012

The Lawrence Housing Authority, Lawrence, MA, Did Not Obtain HUD Approval To Fund a Trust Account And Had Weaknesses in Its Controls

Highlights

Audit Report 2012-BO-1004

What We Audited and Why

We audited the Lawrence Housing Authority, Lawrence, MA, to determine whether it had acceptable management and financial practices to efficiently and effectively administer the use of Section 8 and public housing program funds in compliance with its annual contributions contracts and U.S. Department of Housing and Urban Development (HUD) requirements.

What We Recommend

We recommend that the HUD Director of Public Housing require Authority officials to provide proper supporting documentation to show how the $2.5 million in Federal funds used to fund a trust benefited each Federal program or repay the funds to the Federal program. Also, HUD should obtain a legal opinion identifying whether this trust constitutes an investment, was properly created and whether Federal funds may be used to pay for other post employment benefits. In addition, Authority officials should strengthen their management controls by updating (1) their procurement policy to delegate procurement authority to employees, (2) procedures to prevent interfund accounts, and (3) their methods of tracking force account labor. Also, the updated travel policy should be submitted to HUD and implemented.

What We Found

The Authority generally had acceptable management and financial practices to efficiently and effectively administer the use of HUD Section 8 and Low Income Public Housing Program funds in compliance with its annual contributions contracts and HUD requirements.

However Authority officials did not seek HUD approval to: (1) establish a trust for their other post employment benefits, (2) transfer $2.5 million in reserves to fund the trust, and (3) restrict the use of these funds to the trust exclusive of any other housing-related purpose.

We also found that Authority officials did not properly delegate procurement duties, monitor or prevent interfund borrowing, have adequate procedures for tracking and reviewing the Authority's force account labor projects, and update its travel policy. These events occurred because of specific weaknesses in the Authority's management controls, which affected its ability to manage its operations. As a result, the Authority did not assign procurement duties in writing, have sufficient awareness of interfund imbalances, have a sufficient system to determine whether the use of force account labor was reasonable, or have a travel policy that was adequate. By the completion of the audit, Authority officials had begun to address most of these weaknesses and strengthen their management controls.

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BACKGROUND AND OBJECTIVES

The United States Housing Act of 1937 established the Federal framework for government-funded affordable housing. The United States Congress established public housing to promote the general welfare of the United States by assisting cities, such as Lawrence, in providing decent and safe dwellings for low-income families. The U.S. Department of Housing and Urban Development (HUD) disperses funds to public housing agencies under annual contributions contracts to provide funding for housing assistance for eligible low-income families. HUD provided funding to the Lawrence Housing Authority for 1,055 public housing units in Lawrence, MA.

One amendment to this Act, the Quality Housing and Work Responsibility Act of 1998, created the Housing Choice Voucher program. Under this program, HUD provides funding to public housing authorities to pay rental subsidies directly to multifamily housing owners on behalf of eligible tenants. The Authority administered 1,023 Section 8 vouchers for the City of Lawrence, MA.

For the fiscal years ending March 31, 2010, and March 31, 2011, the Authority received more than $16.3 million in Housing Choice Voucher program funds, more than $8.2 million in operating subsidies for the low-rent housing program, and $3.4 million in capital funds. The annual contributions contracts require the Authority to follow the U.S. Housing Act of 1937, all applicable HUD regulations, and any amendments or changes in the Act or HUD regulations. In addition to the HUD-funded programs, the Authority administered 104 vouchers and operated 522 housing units funded by the Commonwealth of Massachusetts.

The Authority was incorporated on October 26, 1938, under chapter 449 of the Commonwealth of Massachusetts Acts of 1935. The principal staff member of the Authority is the executive director, who was hired by the Authority's board of commissioners, which has served without change in both fiscal years 2010 and 2011. The executive director is responsible for carrying out the policies established by the board and is delegated the responsibility for hiring, training, and supervising his staff to manage the day-to-day operations of the Authority and ensure compliance with Federal and State laws and directives for the programs managed.

We selected the Authority due to the size of its programs and the number of years since our last audit. Our objective was to determine whether the Authority employed acceptable management and financial practices to efficiently and effectively administer the use of Section 8 and public housing program funds in compliance with its annual contributions contracts and HUD requirements.

RESULTS OF AUDIT

Finding 1: The Authority Used Federal Funds To Create a Trust for Other Postemployment Benefit Expenses Without First Obtaining HUD Approval

Authority officials did not obtain HUD approval before they used more than $2.5 million in Federal funds from its Section 8 and low-income housing programs'[1] reserve accounts, to fund a $5.7 million trust for other post employment benefits. Since this type of investment is not specifically allowed according to HUD requirements, HUD approval was necessary. Authority officials mistakenly believed that the trust was approved by HUD because HUD's Real Estate Assessment Center had approved the Authority's audited financial statements. As a result, the $2.5 million is questionable.

Authority Officials Paid $2.5 Million in Federal Funds to a Trust

On February 14, 2012, Authority officials created a tax-exempt trust to be used to pay for other postemployment benefits. Authority officials intended this trust to be an irrevocable trust for the purpose of funding the Authority's other postemployment benefits.[2]

On March 29, 2012, the Authority funded the trust. While the trust documents did not identify which Federal programs provided the funding, a breakdown provided by Authority officials showed that the trust was funded with more than $5.7 million, which consisted of $2.5 million from Federal programs, $1.8 million from the Central Office Cost Center, and $1.4 million from State programs.

The Federal funds invested in the trust came from the public housing operating subsidy, the Housing Choice Voucher program, and the Section 8 moderate rehabilitation programs as follows:

Low-income public housing	Housing Choice Voucher program	Section 8 moderate rehabilitation	Federal programs
$1,933,054	$516,223	$60,897	$2,510,174

[1] Low-income public housing - $1,933,053, Housing Choice Voucher program - $516,223, and Section 8 moderate rehabilitation - $60,897

[2] Other postemployment benefits are part of an exchange of salaries and benefits for employee services rendered. Of the total benefits offered by employers to attract and retain qualified employees, some benefits, including salaries and active-employee healthcare, are paid out while the employees are in active service, whereas other benefits, including postemployment healthcare and other postemployment benefits, are paid out after the employees' services have ended. Nevertheless, both types of benefits constitute compensation for employee services.

Different HUD Programs Have Different Regulations

OMB Circular A-87, codified at 2 CFR (Code of Federal Regulations) Part 225[3] allow payment of postretirement health benefits to a third-party provider (such as a doctor), a third-party insurer, or a third-party trustee maintaining a trust fund for the sole purpose of providing postretirement health benefits to retirees and other beneficiaries. This regulation also allows for amounts funded in excess of that year's actuarially determined other postemployment health plan amount for a fiscal year if that amount is to be used as the government's contribution in a future period. This regulation is silent on dental benefits and life insurance benefits. Public housing operating funds would be subject to this regulation, but Housing Choice Voucher program funds would not. Housing Choice Voucher program funds are further restricted.

For the Housing Choice Voucher program, any administrative fees from fiscal years 2004 through 2012 that are later moved into the unrestricted net assets account at the housing authority's fiscal year end must be used only for activities related to the provision of tenant-based rental assistance authorized under the Section 8 program. In their comments, Authority officials state they used administrative fee reserves prior to 2004, which may be used for other housing purposes and may pay for retiree postemployment benefits. However, Authority officials need to provide documentation showing the amount of administrative fee reserves from 2003 and prior years.

Authority Officials Believed That They Could Use Operating Reserves

HUD has specific requirements for operating reserves. Operating reserves must be maintained by program and are to be used to offset operating deficits in that program. HUD has specific requirements for the management of these operating reserves as well. Excess funds on deposit in operating reserves must be invested in a type of investment security selected by the authority and approved by HUD. These securities, for the purpose of investing operating reserves, must be limited to maturities of 3 years or less. HUD has many different types of allowed investment options, which are listed in HUD Handbook 7475.1; however, trusts are not one of these options.[4] It is, however, possible to obtain HUD approval for investment types that are not listed in the handbook.

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[3]HUD regulations at 24 CFR 85.22, Allowable costs, (b) Applicable cost principles require governmental entities such as housing authorities to use Office of Management and Budget Circular A-87. The Office of Management and Budget codified this circular at 2 CFR Part 225.

[4] HUD Handbook 7475.1, Financial Management Handbook, chapter 5, Operating Reserve, paragraph 3a, Use of Operating Reserves, identifies the limitation on operating reserves, while chapter 4, Cash Management, identifies allowed investment options in paragraph 4.8, Approved Investment Securities

Authority Officials Did Not Ask for HUD Approval

Authority officials did not request HUD approval before using Federal funds to establish the trust. They advised that the payment that moved the funds to the trust did not constitute an investment and that the investment of the funds within the trust follows HUD regulations so HUD approval was not necessary. In the response to this finding (Appendix B) officials also stated they are investing the trust funds in treasury bills with a three month rollover. While Treasury bills invested by the Authority are one of the investment types listed in Handbook 7575.1, we contend that funds paid or transferred to the Trust and invested in Treasury bills in the Trust are an investment outside of HUD. These funds, which are held on behalf of HUD and the Authority, require the direction of the Authority and approval by HUD. .

Authority officials also believed that the Real Estate Assessment Center's approval of the Authority's financial statements constituted approval of the trust, as identified in one of the notes to the financial statements. All housing authorities are required to submit financial statements to the Real Estate Assessment Center. The Real Estate Assessment Center is a division within HUD that reviews the financial statements to determine whether the electronic submission has been successfully submitted to the Real Estate Assessment Center's database and the data are free from mathematical errors. However; financial statements, which include expenditures that are ineligible for Federal programs, may be successfully uploaded to the Real Estate Assessment Center's database,

To properly support any portion of these funds, Authority officials needed to obtain specific HUD approval of the Authority's plans for payment from each Federal program providing the funding. Different Federal programs have different regulations. Expenditures that are eligible for one Federal program may be ineligible for another. The HUD regional field office was unsure whether HUD headquarters would allow the trust and stated that it would seek a determination.

Under 2 CFR Part 225 (Office of Management and Budget Circular A–87), HUD may determine that funds paid from the low-income public housing and Capital Fund programs for health benefits are an eligible expense of the programs, but it is less likely that funds paid from the Housing Choice Voucher program would be an eligible expense unless Authority officials can demonstrate that the funds paid to the trust originated from the administrative fee reserve created with voucher funding received before 2004. In 2004, Congress directed HUD that administrative fee reserves created with voucher funding in 2004 must be used only for the provision of Section 8 rental assistance, including related development activity. Congress has reaffirmed this decision in appropriation bills since 2004.

Conclusion

Authority officials used more than $2.5 million in Federal low income operating reserve funds to create a trust to pay for the other postemployment benefits for its retirees. We contend that without direction or approval by HUD, on the trust's formation and movement of funds to the trust, the 2.5 million is unsupported. Accounting standards require the recognition of this liability, but do not require a trust. Different Federal programs have different rules regarding the use of reserve funds for expenditures. Nevertheless, Authority officials did not request or receive HUD's approval to use Federal funds for this trust. This condition occurred because Authority officials did not believe the movement of funds to the trust constituted an investment, but did believe that the trust was approved by HUD since HUD's Real Estate Assessment Center had approved the Authority's audited financial statements. As a result, we maintain that the 2.5 million is unsupported.

Recommendations

We recommend that the HUD, Director of the Office of Public Housing, Boston Hub require Authority officials to

1A. Provide proper supporting documentation to show how the $2,510,174 in Federal funds benefited and was an allowable expense of each program or repay the funds to that Federal program.

In addition, we recommend that the HUD, Director of the Office of Public Housing, Boston Hub

1B. Obtain a legal opinion identifying whether (1) this trust was properly created and (2) the identified Federal funds may be used to specifically pay for other postemployment benefits, specifically health insurance, dental insurance, and life insurance of retired Authority employees.

Finding 2: The Authority Had Weaknesses in Its Management Controls

The Authority had weaknesses in its management controls. Specifically Authority officials did not properly delegate procurement duties, monitor or prevent interfund borrowing, have adequate procedures for tracking and reviewing the Authority's force account labor projects, or update and implement its travel policy. These events occurred because of specific weaknesses in the Authority's management controls, which affected its ability to manage its operations. As a result, the Authority's procurement policy did not assign procurement duties in writing, the Authority made interfund transfers from the Housing Choice Voucher program, it was difficult to determine whether the use of force account labor was reasonable, and the Authority's travel policy was not adequate. At the completion of the audit, Authority officials had begun to address most of these weaknesses and strengthen their management controls

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Good Management Controls Are Needed

The imposition of good financial management controls is a critical component of any public housing authority's financial management process. Management controls, also called internal controls, are procedures and systems that are designed to provide reasonable assurance of achieving effective and efficient operations, reliable financial and performance reporting, and compliance with applicable laws and regulations.

The Authority did not formally assign procurement duties to Personnel involved in Procurement

Authority officials did not formally assign procurement duties to personnel involved in procurement. HUD Handbook 7460.8, REV-2, paragraph 2.3, entitled Delegation of Authority, requires housing authorities to establish policies for procurement and the delegation of procurement authority. The policy should clearly delegate the limits of the authority in terms of the dollar value of individual obligations the person may make and any other limits (for example, the types of contracts the individual may award, such as small purchases). Delegations should also state whether the recipient may further delegate any of the authority and, if so, how much. Proper delegation of procurement authority protects the Authority from improper procurement actions, overstatement of responsibility, and the appearance of impropriety. While we found no improper behavior in the contracts examined, Authority officials should update the Authority's procurement policies to identify, which employees have procurement authority, clearly state the limits of the authority for each employee, and identify whether re-delegation is allowed.

The Authority Needs To Increase Monitoring of Interfund Accounts

Authority officials did not routinely review interprogram funds to ensure that funds owed from one program to another program were evaluated and eliminated. Officials relied on their financial software for interfund transfers. This software contained features that allowed interprogram fund management and automated reconciliation of downloaded bank transactions. Authority officials did not reconcile these accounts daily, and did not eliminate outstanding balances. Routine evaluation of these transactions would help Authority officials ensure that all expenditures are necessary and properly assigned to their respective HUD program.

Each year, Congress provides funding to HUD to operate specific programs, including the Housing Choice Voucher program, the public housing low-income housing program, and the Single Room Occupancy program. HUD entrusts these funds to public housing authorities through the provisions of the annual contributions contracts to operate these programs. These annual contributions contracts require that program receipts be used only for program expenditures. Each program has a separate annual contributions contract, and funds for that program may not be used for any other program.

The Authority Needs To Strengthen the Monitoring of Forced Account Activity

Authority officials use a force account labor to accomplish many of their capital improvements. Force account labor is labor employed directly by a public housing authority on either a permanent or a temporary basis. For each job using force account labor, Authority officials prepared an initial cost estimate to plan their force account jobs. We found that the prices used in the initial cost estimates were reasonable, but it was harder to determine the reasonableness of jobs where costs increased after the initial cost estimate.

In their 2010 annual plan, Authority officials estimated that $1,974,461 from their 2007 and 2008 Capital Fund grants would be expended. However, funds expended exceeded the estimates by $896,856. This caused authority officials to prematurely draw funds from their 2009 Capital Fund grant. When discussing specific jobs, Authority officials explained that sometimes expenses exceeded estimates due to increases in material costs while other times expenses exceeded estimates due to the type of work being performed. There were also occasions where cost savings allowed the Authority to complete additional projects. Because of the systems used by the Authority, we found that it was extremely difficult to determine the reasonableness of each job that exceeded the initial cost estimate.

Authority officials tracked the expenses of its force account jobs using a commercial accounting software package, spreadsheets, and their general ledger. However; we found no system to track changes to the planned scope of work. HUD regulations do not require change orders for force account jobs; however 2 CFR 225 requires the costs to be reasonable in price. Without a system to show that the increase in the scope of work was reasonable, we were unable to determine that the jobs completed with force account labor were reasonable in price. Establishing a system to track the jobs planned, costs per job, and jobs completed will give the Authority better ability to ensure the reasonableness of the costs.

When we discussed this situation with the executive director, he suggested that the Authority could add a system similar to a contract log to track the cost of jobs completed with force account labor. Such a system would enhance the Authority's management controls and in the long run help the Authority to better control costs of projects using force account labor.

The Authority's Travel Policy Needed To Be Updated

Before the start of our review, Authority officials had a section of its personnel policy devoted to travel expenditures. However, this policy was not adequate because it (1) did not identify the need for preapproval of travel expenses, (2) did not spell out eligible and ineligible expenditures, (3) did not identify fully the documentation necessary to support travel expenditures, and (4) did not identify the relationship of travel to the work of the Authority. After we discussed our concerns with the executive director, Authority officials began changing their travel policy. The new policy

- Identified eligible and ineligible expenditures,
- Provided clear lines of authority regarding the preapproval of travel to conferences and meetings,
- Updated the mileage rates to meet Internal Revenue Service guidelines,
- Updated the meal allowances to meet General Services Administration guidelines, and
- Explained the need for detailed travel expenses and supporting documentation for travel expenses.

Proper implementation of this policy will protect the Authority's interests and prevent abuse of travel expenditures.

Conclusion

The Authority had weaknesses in its management controls. Specifically Authority officials did not properly delegate procurement duties, monitor or prevent interfund borrowing, have adequate procedures for tracking and reviewing the Authority's force account labor projects, or update and implement its travel policy. These events occurred because of inadequate attention to these specific management areas. Therefore, implementing procedures to prevent interfund accounts, formalizing the Authority's procedure into a force account labor policy, and implementing a HUD-approved travel policy would help Authority officials enhance operations and their ability to help the families of Lawrence, MA.

Recommendations

We recommend that the HUD, Director of the Office of Public Housing, Boston Hub require Authority officials to

2A. Update the Authority's procurement policy in writing to ensure that procedures are implemented for delegating procurement authority to employees with clear responsibilities, such as the type and dollar value of procurement allowed.

2B. Establish and implement procedures to regularly review and prevent interfund transactions and provide assurances to HUD that Authority officials will not use Housing Choice Voucher or other restricted funds for purposes other than to pay the expenses of these programs.

2C. Implement a system that allows for review of Force Account cost changes and / or scope of work for reasonableness and develop a better system for tracking and monitoring force account labor and producing timely and comprehensive records on each job.

2D. Submit the revised travel policy that the auditee prepared, for HUD review and implement the policy when approved.

SCOPE AND METHODOLOGY

We conducted the audit between September 2010 and April 2012. Our fieldwork was conducted at the Authority's main office located at 353 Elm Street, Lawrence, MA, and at the maintenance office located at 65 Union Street, Lawrence, MA. Our audit covered the period April 1, 2009, to March 31, 2011, and was extended when necessary to meet our objective. To accomplish our audit objective, we

- Reviewed program requirements including Federal laws, regulations, handbooks, notices, and annual contributions contracts.

- Interviewed the Authority's executive director of occupancy and leasing, chief financial officer, maintenance and operations manager, deputy for management and operations, director of construction and design, and fee accountant.

- Reviewed the financial statements, general ledgers, journal voucher entries, Section 8 administrative plan, annual plans, 5-year plan, and cost allocation plans;

- Reviewed the maintenance purchase order listing of all purchase orders from April 1, 2009, to March 31, 2011, and traced a purchase order to the supporting requisitions and the general ledger detail.

- Reviewed all modernization purchase orders over $2,000 to determine whether purchase orders were sequentially numbered, properly procured, and maintained according to HUD requirements and the Authority's procurement policy.

- Reviewed 7 out of 18 contracts to determine whether the contracts were properly procured and related expenditures were properly supported. The Authority separated its procurement into three categories: maintenance, modernization, and Section 8. We reviewed the four largest maintenance contracts, the largest modernization contract and the two largest Section 8 contracts.

- Selected a representative, nonstatistical sample of 8 of 31 conferences to determine whether the expenses were properly documented, the nature of the conference related to federally subsidized housing, and whether there was a third-party review of the expenditures and supporting documentation. We selected this sample of units without a special reason for including or excluding items.

- Examined the Authority's unrestricted cash, unrestricted net assets, and trust for other postemployment benefits.

- Reviewed the Authority's cost allocations, portability, rent reasonableness, interprogram fund transfers, procurement, and travel to determine whether the Authority officials established and implemented management controls.

- Reviewed the Authority’s procedures for force account labor to ensure compliance with HUD regulations and Davis Bacon wage rates.

- Reviewed Capital Fund program requisitions and supporting documentation to determine whether force account labor was adequately supervised, tracked, and documented.

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

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Controls over use of restricted and unrestricted cash reserves;
- Controls over cost allocations and interprogram accounts;
- Controls over procurement, including the delegation of authority and use of force account labor;
- Controls over travel expenses.

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:

- Authority officials used more than $2.5 million in Federal funds to create a trust for other postemployment benefits without first obtaining HUD approval (See finding 1).

- The Authority had weaknesses in its management controls related to delegating procurement duties, interfund borrowing, tracking, and reviewing its force account labor projects, and implementing updated travel policies (See finding 2).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Unsupported 1/
1A	$2,510,174

1/ 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.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Lawrence Housing Authority
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July 13, 2012

Edgar Moor, Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of the Regional Inspector General for Audit
New England, New York, New Jersey, 2AGA

Dear Mr. Moore:

Please find enclosed responses to the Office of Inspector General for Audit's discussion draft audit memorandum report for your recently completed audit. We appreciate the feedback that was allowed at the exit conference held at this office this morning. We have attached the Authority's formal written comments to the draft memorandum.

We wish to thank the Audit Staff for their assistance and we look forward to the final report.

Very truly yours,

LAWRENCE Housing Authority

Domenic J. O'Neill
Executive Director

EQUAL HOUSING OPPORTUNITY

Ref to OIG Evaluation **Auditee Comments**

Lawrence Housing Authority
Response OIG Audit– Exit Conference
July 13, 2012

Finding 1 The Authority Used Federal Funds to Create a Trust for Other Postemployment Benefit Expenses Without First Obtaining HUD approval

The Lawrence Housing Authority disagrees with this finding.

The Lawrence Housing Authority used program operating reserves from Section 8 and Public Housing that are eligible for use to fund OPEB obligations.

Comment 1

The Authority funded the OPEB liability in a GASB required irrevocable trust to assure compliance with Generally Accepted Accounting Principles (GAAP) and Government Accounting Standards Board (GASB). The Lawrence Housing Authority engaged several third party professionals to give us advice and guidance through the process of compliance to set aside monetary fund's to address this liability.
The funds identified by the Lawrence Housing Authority to pay for OPEB benefits are an allowable operating expense.

Other post employee benefits are identical to retirement benefits that they are earned by employees now to be paid out later. The Lawrence Housing Authority disagrees that the funds used are ineligible under HUD programs regulations.

The Lawrence Housing Authority has adequate administrative fees within the Housing Choice Program, prior to 2004 in the amount of $566,335.00. These fees will be used for funding Housing Choice Voucher's portion of the OPEB.

The Lawrence Housing OPEB Trust Investment Policy currently requires all investments comply with the Investment Policy of the Lawrence Housing Authority. The Funds are currently invested in Federal Treasury Bills with a 3 month roll over back into Federal Treasury Bills. The Authority will recommend to the OPEB Trust that its investments remain in Federal Treasury Bills until we get future clarification. The Authority would like to have its funds invested in the Commonwealth of Mass OPEB Investment Program. This would allow the Authority an opportunity to invest our funds with the State of Massachusetts Health Care Fund. This would provide the Authority with access to top tier investment managers and a larger pool of assets.

Ref to OIG Evaluation **Auditee Comments**

The Authority currently invests its employee pension fund under the similar arrangements with the State of Massachusetts.

The Lawrence Housing Authority feels this finding should be eliminated. The Authority recognizes that the OPEB liability is not simply an issue for the Lawrence Housing Authority but is also one that has significant impact on all government agencies.

The fact that the Lawrence Housing Authority fully funded its OPEB liability should be recognized for whit it is – Sound, prudent cost effective, fiscally responsible use of operating fund. If HUD wants to set policy in direct contradiction to GAAP and GASB with regards to setting up a monetary asset to address the agency OPEB it should set that policy. The GASB statement states that a trust or equivalent arrangement is one in which:

1, Employer contributions are irrevocable

2. Assets are dedicated to providing benefits to retirees and beneficiaries in accordance with the terms of the plan

3. Assets are legally protected from creditors of the employer or the plan administrators. If HUD does not allow Authority to comply with GAAP & GASB it should set such a policy.

The Government Finance Officers Association (GFOA) has stated that the establishment of OPEB Trust is a 2011 Best Practice. HUD should recognize that the Authority addressing its OPEB is a sound cost effective business practice.

Comment 2

The Authority deserves to be given recognition for not only having the financial capacity but the willingness to address this outstanding liability.

Ref to OIG Evaluation **Auditee Comments**

<u>Finding 2</u> **The Authority had Weaknesses in its Management Controls.**

A The Authority did not establish delegation of Authority for Procurement Responsibilities

The Lawrence Housing Authority disagrees with the Labeling of this finding:

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Comment 3

The Authority wants this label changed to:
The Authority did not formally assign procurement duties to Personnel involved in Procurement

The authority to procure goods and services is declared in the job descriptions of specific key employees. The job descriptions are approved by the Authority's Board of Commissioners. The procurement process while not having a formal vote of delegation from the Board of Commissioners or Executive Director is operating properly and follows all the Federal and State procurement rules established by GASB (Government Accounting Standards Board), HUD (Housing and Urban Development) and DHCD (Department of Housing and Community Development). We agree to comply with the OIG's request and ask the Board of Commissioners to formally vote specific positions as eligible to procure for the Authority.

B The Authority Needs to Monitor Inter-fund Accounts

The Lawrence Housing Authority disagrees with the Labeling of this finding:

Comment 4

The Authority wants this label changed to:
The Authority Needs To Increase Monitoring of Inter-fund Accounts

We agree with the increased attention necessary to eliminate and settle inter-fund balances. The funds are currently being balanced and eliminated regularly. The finance department has adopted a timelier consistent schedule suggested by the OIG.

Every Inter-fund charge has always been closely monitored when it is recorded. The accounting software rules have been established assist our review ensuring accurate and consistent recording. Prevention is another matter. The Authority uses a Revolving Fund to facilitate all accounts payable disbursements. The use of a revolving fund requires the use of Inter-fund funds transactions. This process is carefully managed to ensure accuracy. The revolving fund charges each Fund that has requested a payment to be made in its behalf. The funds are transferred after every check run completing and settling any accounts payable inter-company transactions. The use of a revolving fund is an extremely efficient and safe way to control disbursements and vastly streamline the accounts payable function.

Ref to OIG Evaluation	Auditee Comments

Journal entries between funds create an inter-company transaction as well. A monthly transfer of dollars is made to balance and settle any remaining inter-company activity. Once again this process is very closely monitored and the accounting software assists in the review.

The Authority uses an ERP (Enterprise Resource Planning) software called "HAB". It is fully integrated software designed to manage every area of the housing authority's operations. This software comes with a set of tools associated with the software for reporting and analysis of all modules. The finance staff uses these tools to monitor and control all intercompany activity.

Comment 5

The intercompany transfer of $6,573.00 noted within the finding should not have been recognized as a finding. The amount represents a receivable from HUD. The amount was booked as a receivable on the Housing Choice Voucher Program in the amount of $6,573.00 for the Mainstream Program. Both programs use the same cash account. The cash account resides on the Housing Choice Voucher Programs books. The intercompany was settled when we received the from HUD in August 2011.

C The Authority Needs To Track Changes in Forced Account Labor for Reasonableness

Comment 6

The Lawrence Housing Authority disagrees with the Labeling of this finding:

Comment 7

The Authority wants this label changed to:

The Authority Needs To Strengthen the monitoring of Forced Account Activity

The LHA does many of their projects using a Forced Account Process. This process involves the use of key special employees within the Housing Authority to carry out the construction and management of the time and materials projects. The forced account process allows the authority to use their key professional staff to ensure the efficient construction process. The Authority uses both public bidding and forced account to accomplish Capital Improvements. The Authority makes the determination on cost effectiveness and best value when determining which method to use. Size and complexity of the project as well as the capacity of the employees engaged in the project are major factors in the decision.

The choice to do a forced account project is done through analysis and evaluation of the capacity of the LHA's personnel. This initial analysis will determine whether we should contract out the project or continue with a forced account endeavor. The knowledge and quality of the LHA staff has allowed the LHA the opportunity to manage the forced account process more closely and efficiently, when it is the best option. The Authority does a cost benefit analysis to determine what construction method would be the most cost effective and produce the highest quality of the work that would benefit the developments.

Ref to OIG Evaluation | **Auditee Comments**

D The Authority' Travel Policy Needed To Be Updated

The Lawrence Housing Authority agrees with this finding:

Comment 8

The travel was dated and a new policy was developed. The new policy created in November 2011 requires identifying:

1 Eligible and ineligible expenditures

2 Provide clear lines of authority regarding the preapproval of travel to conferences and meetings

3 Updated the mileage rates to meet Internal Revenue Service guidelines

4 Updated the meal allowances to meet General Services Administration guidelines

5 Explained the needs for detailed travel expenses and supporting documentations.

OIG Evaluation of Auditee Comments

Formal comments were received on July 13, 2012 and we made changes to the draft report as appropriate in response to the auditee's written comments. Below, is our evaluation of the comments, referenced in the first part of this appendix where they are presented. The auditee did not agree with any of our recommendations on the OPEB Trust in finding 1, but they did agree with our recommendations to strengthen controls in finding 2.

Comment 1 Congress appropriates funding for HUD annually, and HUD uses this money to fund all of HUD's programs including the Housing Choice Voucher Program. Congress made additional changes in the appropriations laws by rescinding funding for the Operating Subsidy and Housing Choice Voucher programs, as well as issuing new appropriations laws that govern the eligible uses of funds for these programs. These appropriation laws also include instruction to HUD on how the funding may be used. In PIH Notice 12-09, HUD identified that the appropriations law restricts the usage of fees that housing authorities earn under the Housing Choice Voucher Program in that these fees must be used only for activities related to the provision of tenant-based rental assistance. Authority officials used $516,223 in voucher funds to invest in a trust that is designed to pay out future other post-employment benefits to eligible employees who retired from the Lawrence Housing Authority. Prepaying future benefits to retirees is not an eligible expense because it does not provide tenant-based rental assistance to eligible families. As such, this finding will not be removed from the report.

Comment 2 We recognize the efforts of Authority Officials to gain financial capacity and their initiative in protecting the benefits of their retirees, but our concern is that the PHA's investment may not be in the best interest of the program or in compliance with the Appropriations Act provisions and HUD approval should have been obtained in advance of the investment.

Comment 3 We evaluated the auditee's comment, and revised the title of this section of the finding. Nevertheless, the Authority official's actions are responsive to our recommendation.

Comment 4 We evaluated the auditee's comment, and revised the title of this section of the finding.

Comment 5 We agree and we removed the amount but kept the issue in our controls finding, since other years reviewed showed similar weaknesses.

Comment 6 We evaluated the auditee's comment, and revised the title of this section of the finding.

Comment 7 We agree with the auditee's statements on the knowledge and quality their staff and that capital improvements were properly accounted for, however, we maintain; that there should be a system to document reasonableness of additional costs after the initial cost benefit analysis so that it can more easily be determined that changes in the scope and methodology of any force account job are reasonable.

Comment 8 Although Authority officials have updated the travel policy, they need to submit the policy to HUD for review and closure of this recommendation.