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District Inspector General for Audit

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**Audit Memorandum  
No. 2001-PH-0803**

**MEMORANDUM FOR:** Joseph McCloskey, Director, Single Family Asset Management,  
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3AHH

**FROM:** Daniel G. Temme, District Inspector General for Audit,  
Mid-Atlantic, 3AGA

**SUBJECT:** Philadelphia Homeownership Center  
Single Family Disposition Activities  
Philadelphia, Pennsylvania

We have completed a review of the Philadelphia Homeownership Center's (HOC) Single Family (SF) Disposition Activities. The review was performed in response to three external Management and Marketing (M&M) Contractor audit reports issued to the Philadelphia HOC. Specifically, we reviewed the HOC's monitoring controls over the M&M contractors within its jurisdiction and examined the plausibility of using Single Family Acquired Asset Management System (SAMS) data to better monitor SF disposition voucher processing controls, appraisal procedures, and sales to owner-occupant purchasers.

Based on the review, the Philadelphia HOC needs to improve its M&M contractor oversight. Also, HOCs should develop better techniques to utilize SAMS data more effectively in their contractor monitoring and SF housing disposition activities.

Because our review included an analyses of nationwide SAMS data, some of the SF disposition trends we identified appear to have universal applicability throughout the country. Accordingly, the recommendations contained in this memorandum, although addressed only to the Philadelphia HOC, may improve SF disposition activities at the Santa Ana, Denver, and Atlanta HOCs. As such, Headquarters (HQ) should consider implementing the recommendations at all HOCs. Details can be found under the "Results of Our Review" section of this memorandum.

## BACKGROUND

FHA's Single Family Mortgage Insurance Program helps low and moderate-income families become homeowners by reducing down payments and limiting lender fees. Every year, however, thousands of borrowers default on their FHA-insured loans. When they default, FHA encourages lenders to work with them to bring their payments current. When they cannot do this, their homes may be sold to third parties, voluntarily conveyed to the lenders, or surrendered to lenders through foreclosure. Once lenders obtain the properties, they generally convey title to the Secretary of HUD in exchange for payment of their insurance claim.

The National Housing Act of 1934 confers on the Secretary the authority to manage, rehabilitate, rent, and dispose of properties acquired under the Single Family Property Disposition Program. Title 24, Code of Federal Regulations, part 291 implements statutory authority to manage and dispose of acquired properties. Handbook 4310.5, REV-2, dated May 17, 1994, *Property Disposition Handbook - One to Four Family Properties*, supplements the regulations. FHA's Office of Insured Single Family Housing, Asset Management Division, is responsible for administering the program.

As part of HUD's continuing reinvention efforts, FHA issued its 2020 Field Consolidation Plan for Single Family Housing and awarded contracts in March 1999 to manage and market its properties nationwide. The primary contract objectives are to ensure: (1) properties are protected and preserved, properly managed, evaluated, and marketed in a manner which produces the highest possible return to the insurance fund; (2) average losses on sales and the average time properties remain in inventory are reduced; and, (3) the overall program and the image of properties is positive. HUD's primary role is to monitor the M&M contractor's compliance with its contract.

As of March 2001, the Philadelphia HOC SF Housing Real Estate Owned (REO) Branch was responsible for administering five M&M contracts that were awarded to Citiwest (Area 1 - New England), Michaelson, Connor and Boul (Area 2 - Michigan, Ohio, West Virginia and Area 4 - Maryland), First Preston Foreclosure Specialists (Area 3 - New York, New Jersey, Virginia, Washington D.C.), and Golden Feather Realty Services (Area 5 - Pennsylvania). As of February 2001, these contractors were responsible for managing an inventory of over 12,400 properties.

In an effort to increase its monitoring capacity over the M&M contractors, HUD contracted-out for file review and property inspection services. These third party contractors are responsible for reviewing M&M contractor performance in key areas relating to case management and file maintenance, property inspection, maintenance and repair operations. These contractors are required to conduct detailed inspections based on a monthly sampling plan and report the results to HOC REO personnel. In turn, REO staff are required to analyze the results and use the information as one of the key components in preparing its monthly M&M contractor performance assessment. Generally, a randomly selected sample of 10 percent of the properties is selected by HUD and passed on to the contract monitors for detailed inspections. Additional contractual services were acquired to assist in processing and monitoring payment vouchers submitted by M&M contractors.

## Automated System

The Single Family Acquired Asset Management System (SAMS) is HUD's automated system that provides data for management, processing, and monitoring of acquired and custodial single family properties. SAMS is designed to facilitate the processing of properties through disposition and to perform a variety of accounting functions. The case management process within SAMS records all data associated with the acquisition, maintenance, and disposal of single family properties. The case management process also allows HUD management to monitor the timely processing of properties. For financial management, SAMS records accounting information regarding tax payments, other accounts payable, cash disbursements and collections. SAMS also provides general accounting information, including total direct costs of property disposition. SAMS tracks 10 case management processing steps, beginning with the acquisition of a property and ending with the reconciliation of funds from the final sale or disposal of the property.

## **Prior Audits**

During FY 2000, we conducted separate audits of the three M&M contractors (Citiwest; Michaelson, Connor and Boul; and First Preston) assigned to manage the Philadelphia HOC's property inventory in areas 1, 2, and 3.<sup>1</sup> In September 2000, the OIG issued three audit reports that addressed internal weaknesses in the property inspection and maintenance, voucher processing, and property case management disposition operations of these three M&M contractors. These audits were part of a nationwide M&M contractor assessment the OIG performed of five M&M contractors at all four HOCs. The results of each audit were summarized in an overall report to HQ, also issued in September 2000.

## **OBJECTIVES, SCOPE AND METHODOLOGY**

Our primary objective was to evaluate the effectiveness of the Philadelphia HOC's M&M contractor monitoring and follow-up procedures. Additional objectives were to obtain relevant nationwide SAMS data and determine if adequate controls were in place to ensure payments to M&M contractors were proper; to examine SF REO appraisal data and the appraisal monitoring process; and to survey owner/occupant home sales.

To meet our objectives, we:

- Interviewed HOC, REAC, contractor, and private industry REO and appraisal officials;
- Reviewed HOC monthly M&M contractor performance assessment reports;
- Reviewed third party contractor prepared inspection reports;
- Reviewed HUD monitoring guidelines and disposition policies and procedures;

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<sup>1</sup> Additional contracts were awarded to Michaelson, Connor and Boul (Area 4), and Golden Feather (Area 5) after the M&M contractor audits commenced.

- Analyzed all pass-through costs processed nationally by M&M contractors and HUD;
- Reviewed a judgmentally selected sample of payment vouchers and supporting documents; and
- Obtained and analyzed nationwide SAMS payment, appraisal, bid, non-profit sales, and settlement data.

## **RESULTS OF OUR REVIEW**

We found that the HOC needs to strengthen its M&M contractor monitoring and follow-up procedures to ensure that significant and recurring performance deficiencies identified in prior audits and by third party contract monitors are reported and more closely monitored and tracked. Further, voucher processing and file maintenance controls need improvement to minimize the processing of duplicative pass-through and incorrectly computed fixed-fee payments.

Because some HOC REO personnel often had other priorities to manage and did not fully understand how to use inspection information provided by third party contract monitors, performance deficiencies were not always reported, nor were methodologies established to track the development and progress of corrective actions. Additionally, HOC staff were ill-equipped to manage the voluminous amount of paperwork associated with M&M contractor voucher submissions, and often implemented manual overrides to force the automated system to process vouchers that could not otherwise be processed.

As a result of not fully implementing monitoring and follow-up procedures, M&M contractor performance deficiencies were not corrected and subjected HUD to the higher risks associated with poor property conditions such as decreased marketability, increased holding costs, negative impact on surrounding communities, and public health and safety concerns. Also, weak voucher processing controls resulted in potentially duplicative pass-through payments totaling over \$937,000<sup>2</sup>. Further, automated system limitations resulted in incorrect payments for fixed-fee vacant lot transactions and inappropriate manual fee adjustments when properties were listed and closed within the same month.

Although new policies, procedures, studies, and changes to the M&M contracts promulgated by HQ in response to the OIG's nationwide audit of HUD's SF Property Disposition Program will likely improve the program and the monitoring of M&M contractors, our review disclosed that the HOC should establish and maintain an effective performance monitoring and tracking system, and should consider the use of SAMS data and automated techniques to assist in its monitoring of SF disposition activities.

Our review also showed that better use and analyses of relevant SAMS data would likely improve the HOC's M&M contractor oversight capability. Application of these techniques should improve the HOC's ability to detect non-performance of key contract requirements, quantify the effect, and identify and measure performance trends so that vulnerabilities can be

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<sup>2</sup> An additional \$860,000 in potentially duplicative pass-through costs were also identified that were processed by the Santa Ana, Denver, and Atlanta HOCs.

better assessed, and limited monitoring resources more appropriately directed. Our analyses of the data, and comparisons of appraisal values and sales prices, and limited testing of owner-occupant sales, indicated that HUD should be concerned about the quality of SF REO appraisals and the high potential for special sales program abuse.

#### M&M Contractor Monitoring and Follow-up Need Improvement

In accordance with monitoring guidelines, REO staff are required to review M&M contractor performance on a monthly basis employing a 16 step monitoring process plan. In general, the plan requires:

- gathering background information;
- obtaining third party contract inspector reports;
- conducting monthly site visits;
- completing performance and risk analyses for each deficiency;
- identifying of potential corrective actions;
- preparing a performance assessment report;
- obtaining M&M contractor responses;
- determining final corrective actions; and
- establishing an ongoing corrective action verification plan.

In order to assess the HOC's monitoring and follow-up procedures, we reviewed 27 monthly performance assessment reports prepared by REO personnel during the 9 month period, January through September 2000, (one per month for each of the three M&M contractors). We also reviewed 12 file review inspection reports for the period May through August 2000, and 12 special property inspection reports for the period June through September 2000 prepared by third party contractor monitors (four months for each of the three M&M contractors). Our review showed that the HOC's assessment reports generally did not include the results of site visits; document the results of risk analyses; identify corrective actions; and indicate the development of a corrective action and follow-up plan. The review also showed that although third party contract monitors consistently reported the same key performance deficiencies from month to month, the HOC did not effectively use this information to report and correct deficiencies in its monthly assessments of M&M contractor performance.

#### HOC Assessments Did Not Include Risk Analyses or Corrective Actions and Follow-up Plans

Our analyses of the 27 monthly HOC assessment reports prepared during the 9 month period ending September 2000 showed that while some performance concerns were documented, the reports did not include or make use of many of the key monitoring components as specified in the monitoring guidelines. Specifically:

- only 20 of 27 site visits were conducted (the recommended site visit frequency was once per month).

- of the 98 findings identified in the reports, there did not appear to be any effort to assess the risks associated with reported deficiencies and identify potential corrective actions.
- we did not find any evidence that a corrective action plan was established to monitor and track efforts to correct the 98 findings and improve M&M contractor procedures.

Because corrective actions were not identified and tracked, performance deficiencies were not rectified and often recurred from month to month. For example, of the 98 findings, 73 (74 percent) were repeated during our period of review. We also determined that, although third party contract monitoring services were obtained to increase the HOC’s M&M contractor monitoring oversight, the results of their inspections were not effectively used by the HOC in performing its assessment of M&M contract operations.

Third Party Contract Monitor Reports Not Effectively Used

Our review of the 12 monthly file reviews and 12 special property inspection reports showed that M&M contractor performance deficiencies in key areas were consistently identified from month to month, but were not used by the HOC and reported in its assessments to the M&M contractors. For example, the 12 file review reports identified 174 problem areas in 23 key contract performance areas. Of the 174, 91 problem areas (52 percent) were identified as recurring during our period of review. Although problems were identified and reported by third party contract monitors, only 22 of the 174 problem areas were subsequently reported to M&M contractors through HOC assessment reports. Review results are summarized as follows:

**Summary of File Review Inspection’s Results**

	<b>First Preston</b>	<b>MCB</b>	<b>Citiwest</b>	<b>Total</b>
Problem Areas Identified By File Review Inspectors	64	65	45	<b>174</b>
Unresolved Problem Areas Recurring from Month to Month	29	40	22	<b>91</b>
Problem Areas Reported in HOC Assessments	4	4	14	<b>22</b>

A more detailed summary showing the types of file review findings by month and M&M contractor is attached as Appendix A.

A similar analyses of 12 monthly special property inspection reports indicated that the M&M contractors were doing a poor job of maintaining HUD’s property inventory. While the unsatisfactory results were generally reported in the HOC assessments to the M&M contractors, high unsatisfactory ratings were repeatedly identified from month to month. The percent of inspections that resulted in unsatisfactory ratings during the 4 month review period are summarized as follows:

### Unsatisfactory Property Inspection Result Percentages

	First Preston	MCB	Citiwest
June	65%	38%	43%
July	67%	54%	76%
August	69%	52%	77%
September	80%	83%	49%

Despite REO personnel reporting the poor quality of inspection, maintenance and repair procedures used by the M&M contractors, third party contractor monitor results clearly showed that except for the Citiwest September results, property conditions were getting worse instead of improving. Unless the results of third party contract monitors are effectively communicated to the M&M contractors and a corrective action identification and follow-up plan is established and implemented, performance problems are likely to continue.

#### Causes

Our discussions with responsible HOC REO personnel revealed that travel fund limitations prevented M&M contractor site visits. Additionally, workload requirements and other priorities precluded detailed risk assessments, corrective action identification, and follow-up. We were told that REO staff were barely able to produce a monthly report, and did not have the resources and training to perform detailed risk assessments, and establish and implement a tracking and follow-up plan. REO personnel also stated that they did not have the time to fully analyze third party contract monitor inspection documentation. In some cases, responsible personnel did not review the reports because they did not understand the results and did not know how to use them as part of the overall M&M contract monitoring process.

According to a 1997 Andersen Consulting study, a full-time HUD employee should be able to monitor the management and sale of 70 properties when those functions are performed by contractors. Our analyses of REO and Program Support Branch staffing assignments and property inventory levels showed that each available staff member was responsible for managing about 319 properties. While this analyses appears to support staff claims of insufficient resources, we believe this stresses even more the importance of assessing risks, identifying corrective actions, and establishing an effective follow-up plan. Rather than completing monthly assessment reports just to meet monitoring requirements, careful analyses of the identified problem areas should be done so that scarce resources can be more appropriately directed to solve systemic problem areas and to better ensure HUD's interests are protected. Further, since a significant portion of the monitoring workload has been outsourced, third party inspection results should be used to the maximum extent practical.

## HOC Voucher Processing Procedures Need Improvement

In our prior audits of the three M&M contractors operating within the jurisdiction of the Philadelphia HOC, we identified voucher control weaknesses that resulted in the processing and payment of ineligible and duplicate pass-through costs. The recommendations made as a result of these audits should improve contractor voucher processing controls and reduce the risk of ineligible and duplicative payments. We also discovered that fixed-fee payments for transactions involving vacant lots were incorrectly computed because of SAMS limitations, and manual adjustments were erroneously submitted and processed when properties were listed and sold within the same month. Vouchers and manual adjustments are ultimately reviewed and approved for payment at the HOC; therefore, we believed an assessment of HOC voucher processing controls was needed. To facilitate our review, we obtained nationwide SAMS pass-through voucher payment data from October 1999 through August 2000. During this period, HUD processed 2,806 vouchers containing 144,844 line items and paid about \$72.6 million in pass-through costs to M&M and other contractors, such as asset managers, appraisers, closing agents, and title reviewers involved in the SF REO disposition process.

Using Computer Assisted Audit Tools (CAATs), we analyzed the 144,844 line items to determine if there were indications that pass-through costs were paid more than once. We considered a line item payment potentially duplicative if the property case number, line item amount, and post code (identifies the service being paid for) were the same. The analyses showed that 10,756 line items valued at about \$3.2 million were potentially duplicative. Details summarized by HOC are as follows:



### Nationwide Potential Duplicate Pass-through Payments

<b>Homeownership Center</b>	<b>Line Items</b>	<b>Dollar Amount</b>
Philadelphia	2,956	\$1,188,346
Santa Ana	4,809	693,953
Denver	185	14,047
Atlanta	2,800	614,949
Headquarters	6	680,616
<b>Total</b>	<b>10,756</b>	<b>\$3,191,911</b>

For a more detailed property and description summary by HOC, see Appendix B.

In order to determine if duplicate payments were made and to evaluate Philadelphia HOC voucher processing procedures, we judgmentally selected for detailed review 62 voucher transmittal packages<sup>3</sup> that included 116 vouchers and 179 of the potentially duplicate line items. Because the HOC did not have adequate physical control over its voucher files, they could only locate and provide 10 of the 62 packages. Vouchers were haphazardly stored in filing cabinets, desk drawers, and boxes. Basic record keeping procedures were not established. Consequently, a detailed duplicate assessment could only be performed on 13 vouchers and 43 line items. Our review of the 43 line items showed that:

- 5 line items were not duplicate payments.
- 12 line items were processed in duplicate.
- 26 line items could not be sufficiently evaluated because the items were not processed by property case number as required. Instead, each line item represented a summarized invoice total of costs for numerous case numbers. Thus, we were unable to determine if a duplicate cost was paid for a specific property. We were told that the HOC sometimes processed charges for several properties in bulk on one voucher line because it was the most expedient method of payment.

Based on our detailed review and discussions with HOC voucher processing personnel, we determined that line items were processed more than once primarily because staff were not capable of dealing with the volume of paperwork associated with voucher submissions and placed priority on getting the voucher paid instead of performing eligibility validations. For example, the 12 line items we substantiated as being paid incorrectly more than once resulted from HOC personnel manually creating or modifying missing invoice numbers in SAMS, effectively circumventing system controls to prevent duplicate processing of invoices.

#### Likely Eligible Payments

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<sup>3</sup> A voucher transmittal package grouped the same potential duplicate line items together and included the transmittal, voucher, and all supporting invoices and documentation.

Based on our detailed review and discussions with HOC personnel, we determined that some of the potentially duplicative payments we identified could represent legitimate payment for services that were of a recurring nature. Accordingly, we eliminated from our potential duplicate payment list those post code categories associated with homeowner association and condominium, utility, property inspection, and file review fees (post codes CF, UT, IF and FR, respectively). Because of the recurring nature of these costs, it would not be unreasonable to expect that the same property might incur costs that are identical in amount and for the same type of service. Removing these post code categories from our original list revealed that 3,519 potentially duplicate line items valued at about \$1.8 million remained. Details by HOC are as follows:

**Nationwide Potential Duplicate Pass-through Payments After Eliminating Likely Eligible Items**

Homeownership Center	Line Items	Dollar Amount
Philadelphia	671	\$ 937,280
Santa Ana	583	274,270
Atlanta	2,224	578,830
Denver	41	7,372
<b>Total</b>	<b>3,519</b>	<b>\$1,797,752</b>

These remaining suspect duplicate payments should be reviewed by the HOC to determine their eligibility. If duplicate payments are verified, then appropriate actions should be initiated to obtain reimbursement. To facilitate the review, detailed reports of the 3,519 potentially duplicative payments were provided to the Philadelphia HOC for dissemination and appropriate action for all HOCs.

**M&M Contractor Fixed-Fee Payment Processing Issues**

M&M contracts prescribe that contractors will be paid a fixed-fee for managing and marketing an assigned property inventory. Depending on the property category, an applicable pricing factor is multiplied by the listing and final sales prices to determine the amount due to the contractor. Fixed-fees are payable in two installments; first, when a property is listed for sale; and second, when the property is sold. Separate pricing factors are used for improved properties, vacant lots, custodial, and rental properties. SAMS automatically computes the fixed-fee payments.

We noted that SAMS limitations and incorrectly processed manual adjustments precluded accurate payment in certain circumstances. For example:

- vacant lot pricing factors were not loaded in SAMS and improved lot pricing factors were used instead to calculate the fixed-fee payment. Our discussions with SAMS’ personnel revealed they were aware of this issue and decided not to make the required program changes since so few vacant lots were in inventory. We were also told that vacant lot payments should be manually adjusted to ensure proper payment. In one contractor’s case, the vacant lot-pricing factor is 3.6 percent less than the improved lot

factor. Therefore, the contractor would be overpaid for vacant lot listings and sales. Both HOC and contractor officials were not aware that fee payments for vacant lots needed to be manually adjusted.

- for properties that were listed and sold during the same month, SAMS would automatically process both the first and second installment payment on a single line and code the payment as the second installment. One M&M contractor assumed that payment was only made for the second installment and would process a manual adjustment to obtain the first installment fee. In this circumstance, the contractor could be paid twice for the first installment.

During FY 2000, the Philadelphia HOC procured the services of T. Curtis and Associates to perform voucher reviews. While this should help ensure that more diligent voucher and manual adjustment reviews are performed, the HOC needs to establish and maintain an effective voucher filing system, train its personnel in proper voucher review techniques, and should consider the use of SAMS data and automated techniques to ensure ineligible payments are discovered, and procedures are instituted at the HOC and at the contractor level to minimize this occurrence.

### SF Property Appraisals

Obtaining high-quality property appraisals and accurate assessments of a property's market value is critical to HUD's SF disposition process, and is used by HUD as a critical element in measuring program performance. In managing HUD's SF property inventory, M&M contractors are required to obtain property appraisals from HUD-approved appraisal companies. Since the appraised value is used to establish the property's list or asking price, the appraisal directly affects a property's marketability, and is a key factor in determining the amount and timeliness of an M&M contractor's fee payments. Consequently, the appraisal process is inherently vulnerable to abuse and should be closely monitored.

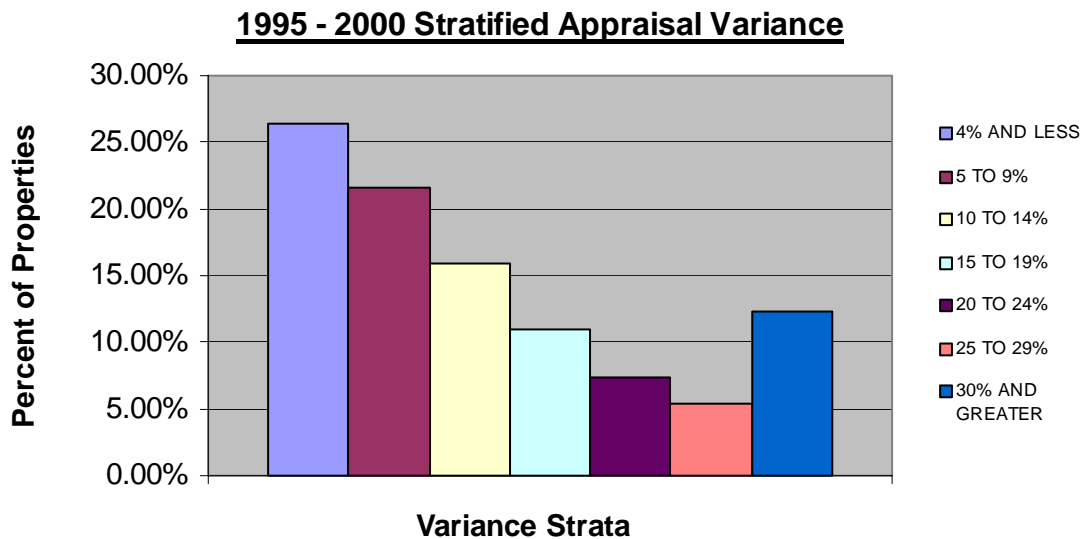
### Appraisal Process Not Monitored

Contract specifications require M&M contractors to develop and submit for HUD approval an appraisal monitoring and quality assurance plan. Discussions with HOC personnel revealed that they were neither aware if plans were received and reviewed, nor cognizant of the status of any ongoing quality assurance measures performed by the M&M contractors. Further, responsible personnel told us that the SF REO appraisal process had received virtually no HUD oversight. In its response to our prior nationwide audit of the SF Property Disposition Program, HUD recognized the need to implement additional controls over the REO appraisal process, and indicated that an automated appraisal scoring system and quality assurance program would be developed by the Real Estate Assessment Center. Our discussions with REAC personnel revealed that the project is in its preliminary development phase. Because of the inherent risks associated with the SF REO appraisal process and the lack of HUD oversight, we obtained nationwide SAMS appraisal and sales data, and used CAATs to assess the quality of SF REO appraisals and performed limited trend analyses. Our review of the appraised values and sales

prices for 188,486<sup>4</sup> properties sold from January 1995 to October 2000 showed that the quality of the appraisals was highly questionable and that some alarming trends were readily apparent.

Quality of SF REO Appraisals Appears Questionable

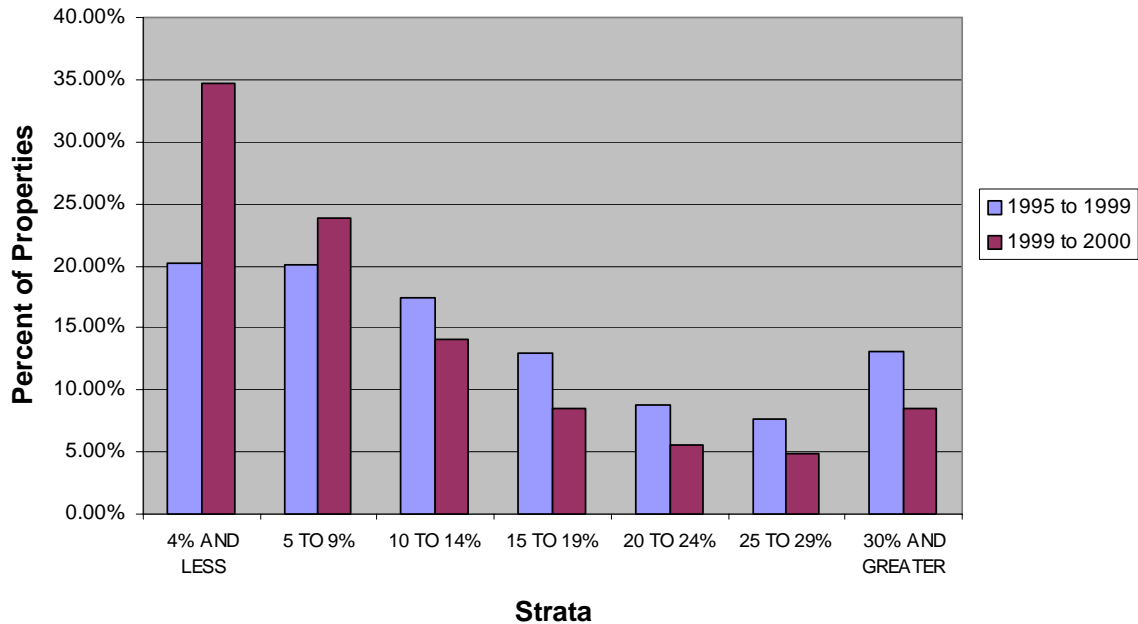
In order to assess the quality of SF REO appraisals, we compared the appraised value of the 188,486 properties in our database to the sales price and computed the percent appraisal variance (difference between the appraised value and sales price, divided by the appraised value). Our analyses revealed that over 23,000 (12 percent) of the appraisals varied by 30 percent or more of the sales price. Stratified variance results are summarized as follows:



To determine if there was any correlation of the quality of the appraisals from the time before and after the award of the M&M contracts, we compared our pre-M&M contract results (1995 to 1998) to the results after contracts were awarded (1999). The analyses showed that the percent of appraisal variance averaged about 16 percent before contracts were awarded and about 12 percent after award. Stratified appraisal variance results before and after M&M contract awards were as follows:

<sup>4</sup> To mitigate the effect of HUD policies and special sales programs that would impact a property’s selling price, we excluded from our review those properties that were sold as a result of bulk, direct, Officer Next Door/Teacher Next Door, and other non-profit sales programs. Further, we included only those properties that had a disposition code entry and whose sales record could be matched with an appraisal record.

### Before / After M&M Contract Award - Stratified Appraisal Variance



We researched private industries whose reliance on the SF property appraisal and disposition process was critical to achieving company goals and objectives similar to those of FHA (maximizing sales returns in the most efficient manner). Our research disclosed that a performance measurement used to assess the quality of an appraiser's work was to ensure that 65 percent of an appraiser's completed assignments fall within 4 percent of the appraisal variance, as computed in our analyses. As the charts above indicate, only 26 percent of the total SF REO appraisals were within a 4 percent variance. Although the quality of the appraisals completed under the M&M contractors appears to be better since 35 percent of their appraisals were within the 4 percent variance benchmark, they still fall well below industry goals and objectives. Further analyses of the appraisal data identified other alarming trends.

### High Volume of Appraisals Prepared By a Few Companies

Summarizing the appraisal data by preparer showed that 623 companies completed the 188,486 appraisals included within the scope of our nationwide review. Frequency analyses showed that the top 10 companies were responsible for preparing about 79 percent of the appraisals. The number one company alone completed 67 percent. The appraisal variance of these companies averaged about 15 percent. Details were:

### Appraisal Frequency By Company and HOC

RANK	APPRAISAL COMPANY	NUMBER OF APPRAISALS	PERCENT OF TOTAL	AVERAGE APPRAISAL VARIANCE	HOMEOWNERSHIP CENTER			
					ATL	DEN	PHL	SAN
1	<b>FIRST AMER. APPRAISAL SER.</b>	<b>126,074</b>	<b>66.89%</b>	14.78%	X	X	X	X
2	RAY J SKOCHKO REAL ESTATE APPR	4,548	2.41%	10.43%				X
3	WALTER MATTHEWS & ASSOC INC	3,941	2.09%	17.46%	X			
4	APPRAISERS OF TULSA	3,208	1.70%	14.75%		X		
5	ANTHONY G CONTRERAS & ASSOCIATE	3,084	1.64%	11.64%				X
6	DEBRA J BLINDMAN APPRAISAL CO	2,805	1.49%	12.84%		X		
7	ATLANTA APPRAISAL SERVICES LLC	1,434	0.76%	16.06%	X			
8	MARY PETERS & ASSOCIATES APPRA	1,287	0.68%	13.34%	X			
9	WIETIES & BECK INC	1,155	0.61%	17.28%	X			
10	MTB INVESTMENTS INC	1,045	0.55%	15.13%	X	X	X	
	<b>TOP 10 APPRAISERS - TOTALS</b>	<b>148,581</b>	<b>78.83%</b>	<b>14.64%</b>				
	<b>ALL 623 APPRAISERS - TOTALS</b>	<b>188,486</b>	<b>100.00%</b>	<b>14.34%</b>				

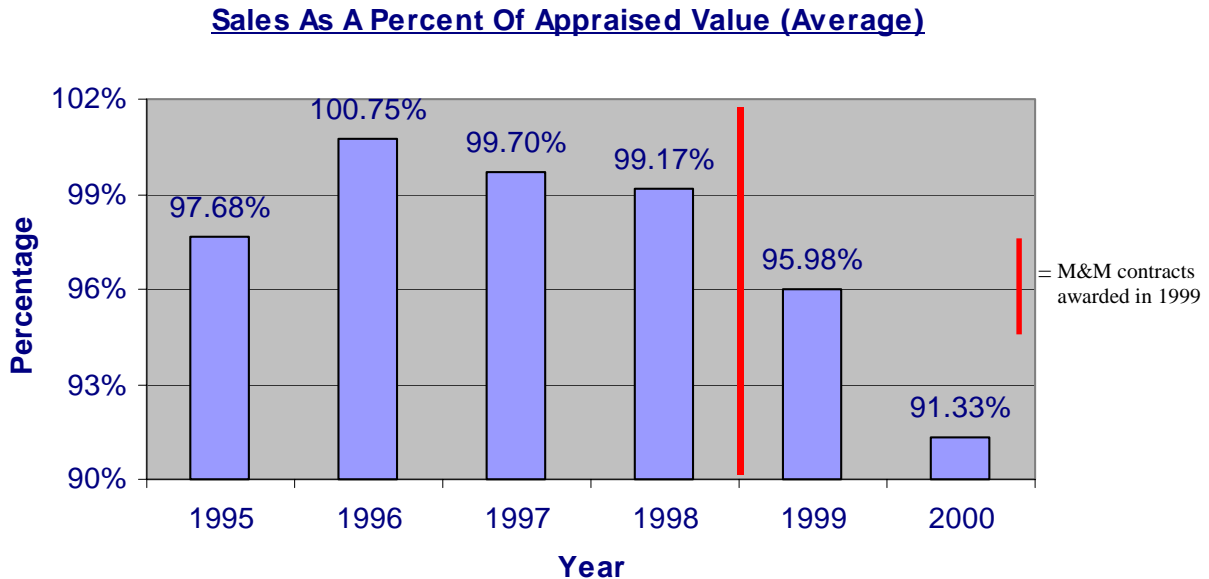
This analyses suggests that initial appraisal monitoring and quality assurance efforts might best be focused on these companies and HOCs.

#### Key FHA Objective Not Met by M&M Contractors

One of the objectives by which FHA measures SF Property Disposition Program performance is to sell its properties at 98 percent of appraised value. Using the SAMS appraisal and sales data we obtained for the 188,486 properties included in our analyses, we determined the average appraisal values and sales prices from January 1995 through October 2000 and computed the average sales as a percent of appraised value. Average appraisal and sales figures are as follows:

YEAR	PROPERTIES SOLD	AVERAGE APPRAISAL VALUE	AVERAGE SALES PRICE	DIFFERENCE	PERCENT OF APPRAISAL
1995	7,510	\$60,444.52	\$59,042.74	(\$1,401.78)	97.68%
1996	23,183	\$60,149.23	\$60,600.02	\$450.79	100.75%
1997	37,942	\$61,565.36	\$61,381.32	(\$184.04)	99.70%
1998	39,881	\$65,282.68	\$64,742.87	(\$539.81)	99.17%
1999	42,749	\$75,325.93	\$72,296.20	(\$3,029.73)	95.98%
2000	37,221	\$75,783.94	\$69,210.57	(\$6,573.37)	91.33%

Notwithstanding the previously discussed concerns over the quality of the appraisals, our analyses showed the average sales as a percent of appraised value in the years prior to the award of the M&M contracts were generally within the 98 percent program objective. However, performance has significantly deteriorated since HUD’s SF inventory has been managed by the M&M contractors, graphically depicted as follows:



As the Department prepares to fully assess the SF REO appraisal process, our analyses suggests that additional study of the M&M contractor’s role in impacting the sales as a percentage of appraisal performance measurement is highly warranted to prevent further declines.

Abuse of the Owner-Occupant Sales Program

An integral component of HUD’s SF disposition goals is to reduce the property inventory in a manner that expands homeownership opportunities and strengthens neighborhoods and communities. While both owner-occupant and investor purchasers may acquire HUD-owned properties, sales procedures are designed to enhance opportunities for owner-occupant buyers. When HUD properties are listed for sale, an initial 10 day bidding period is established and is open only to buyers intending to purchase the properties as an owner-occupant. Since 1998, eligibility requirements included certifying that (i) no other HUD-owned property has been purchased in the last 24 months as an owner-occupant; and, (ii) the property will be occupied as the primary residence for at least 12 months. Prior to 1998, 12 month residency was the only requirement. If an acceptable owner-occupant bid is not received within the initial 10 day period, bidding is opened-up to investors and other prospective buyers.

Because HOC personnel told us owner-occupant sales were not specifically monitored to ensure buyers were in compliance with program and eligibility requirements, we used CAATs to analyze

124,447 owner-occupant and 44,020 investor purchases<sup>5</sup> valued at \$9 billion and \$2 billion, respectively, made during the period January 1995 to October 2000. We designed our analyses to isolate buyers with multiple owner-occupant purchase activity and to determine the extent of individuals purchasing both as an owner-occupant and investor. Our analyses showed that 2,124 buyers had acquired more than one property as an owner-occupant, stratified as follows:

**Owner-Occupant Buyers With Multiple Purchase History**

<b>PROPERTIES PURCHASED</b>	<b>NUMBER OF BUYERS</b>	<b>NUMBER OF PROPERTIES</b>	<b>TOTAL VALUE</b>
4 or more	97	505	\$ 25,520,862
3	242	726	37,680,311
2	1,785	3,570	217,853,858
<b>Total</b>	<b>2,124</b>	<b>4,801</b>	<b>\$ 281,055,031</b>

A single buyer with multiple purchase history as an owner-occupant can be indicative of program abuse since residency requirements may not have been met and buying frequency may have been exceeded. To test the purchase frequency, we further analyzed the 4,801 properties acquired by the 2,124 buyers with two or more purchases to determine if the properties were purchased after 1998 and within 24 months of each other. This more detailed analyses showed that 1,434 (30 percent) of the properties valued at \$96 million were purchased in apparent violation of the frequency limitation.

Our analyses also showed that a significant number of sales were made to buyers acquiring properties both as an owner-occupant and investor. We identified 2,986 buyers who purchased 4,040 homes as an owner-occupant and 9,787 homes as an investor during our period of review. Total value of these 13,827 properties was over \$721 million. In one case, the same buyer purchased 15 properties as an owner-occupant and 30 as an investor. Some examples of the most egregious cases and the buyer's annual buying frequency are as follows:

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<sup>5</sup> Our analyses only included those purchases that were: (i) made by individuals; (ii) coded as owner-occupant or investor; and (iii) associated with a social security number.



BUYER	OWNER - OCCUPANT PURCHASES	INVESTOR PURCHASES	ANNUAL PURCHASE FREQUENCY ( OWNER-OCCUPANT - INVESTOR )												TOTALS		
			1995		1996		1997		1998		1999		2000				
A	15	30					11	22	4	8							45
B	8	29	3	2		5	5	4		10		1			7	37	
C	8	58		7	2	4	4	11	1	14	1	3		19	66		
D	7	123		1			3	18		30	2	24	2	50	130		
E	6	60				17	1	13				18	5	12	66		

As our analyses and the above charts depict, it appears that a significant number of purchasers are abusing the program and depriving other potential buyers of homeownership opportunities. In order to ensure housing benefits are provided only to qualified beneficiaries and FHA objectives relating to providing expanded housing opportunities are maximized, HUD should implement tighter controls over its owner-occupant sales process.

\* \* \* \* \*

As the Department continues to improve its monitoring policies and procedures over the SF Property Disposition Program, it should explore all available options to maximize oversight capability and efficiency, particularly in light of limited resources. As our review demonstrates, a viable option is to make better use and analyses of relevant SAMS data utilizing specialized automated techniques. Employing the use of these techniques should improve the HOC’s ability to identify program vulnerabilities and systemic weaknesses so that scarce resources can be more efficiently guided.

Recommendations:

We recommend you:

1A. Complete detailed risk assessments of problem areas identified as a result of implementing M&M contractor monitoring procedures. Use the risk assessment results to prioritize the direction and application of monitoring resources and conducting on-site inspections. For those areas determined to be of a higher priority, work closely with the M&M contractors to:

- determine the causes of the problem;
- develop corrective actions;
- establish and implement a corrective action follow-up plan; and
- monitor and track contractor efforts to correct deficiencies.

- 1B. Provide training to staff assigned M&M contractor monitoring responsibilities to ensure they understand how to interpret and use inspection results provided by third party contract monitors.
- 1C. Establish and maintain a filing system for vouchers submitted by contractors for HUD's review and payment approval. At a minimum, procedures should be established to ensure maintenance of receipt, sign-in/sign-out, disposition logs and adequate storage facilities.
- 1D. Improve voucher review and approval procedures to minimize the payment of duplicate line items. Ensure contractor submitted vouchers and line item charges are:
- processed and supported with original pre-numbered vendor invoices;
  - properly coded with the appropriate post code; and
  - not processed in bulk to the maximum extent possible.
- 1E. Review the list of 671 potentially duplicative pass-through line items valued at \$937,280 provided by the OIG and perform detailed eligibility validations of the charges. For those line items determined to be duplicative, HOC personnel should initiate actions to seek reimbursement from the applicable contractor.
- 1F. Carefully review manual adjustments submitted for fee payments for properties that are listed and sold during the same month to ensure M&M contractors were not overpaid.
- 1G. Develop procedures to periodically analyze relevant SAMS payment, appraisal, settlement, and special sales program data to identify incorrect payments, quality, performance, and program eligibility and compliance trends. Where applicable, use analyses and trend results to develop and implement new monitoring procedures or improve existing procedures.

The results of our review were discussed with HOC officials during the review and at an exit conference held on April 27, 2001. HOC officials stated they agreed with the review and have initiated actions to implement the recommendations made in this audit memorandum. We have included the HOC's response as Appendix C.

If you have any questions, please contact Cliff Cole, Assistant District Inspector General for Audit at (804) 278-4500, extension 3794.

### Summary of Third Party Contractor File Review Inspection Results

DESCRIPTION	MAY									JUNE								
	FIRST PRESTON			MCB			CITIWEST			FIRST PRESTON			MCB			CITIWEST		
	735 FILES REVIEWED			219 FILES REVIEWED			120 FILES REVIEWED			816 FILES REVIEWED			193 FILES REVIEWED			114 FILES REVIEWED		
	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B
27011A RECEIVED	7			18			4			13			9	1		11	1	1
27011A DAMAGE CLAIMS				104						1			64	1				
PART B REVIEW										5			111	1				
INITIAL INSPECTION DATE	60									70			5			5		
FILES COMPLETE AND ACCURATE				216			14			793			191			40		
DEED REQUEST	253			7									10					
NOTATIONS TO TAX AUTHORITIES	328			217						339	1		188	1		12		1
PRESERVATION AND PROTECTION	514			5			1			559	1		10	1		12	1	
HAZARDOUS CONDITIONS	2			18						7			13	1		1		
HAZARDOUS MATERIALS REMOVED	2																	
EMERGENCY REPAIRS	4									8						3		
MAJOR REPAIRS	38									32	1					5		1
APPRAISAL IN FILE	62			12						41	1		4	1		13		
APPRAISAL DATE RECEIVED	12			33						15	1		11	1				
APPRAISED WITHIN 10 DAYS	341		1	99		1	28			401	1	1	81	1	1	55	1	1
DEFECTIVE PAINT CERTIFICATION	55			14						41	1		3	1		17		1
FILE DOCUMENTATION MAINTAINED	9									7								
INSPECTION WITHIN 24 HOURS	351			101			20		1	411	1		76	1		48	1	1
SUBSEQUENT INSPECTION DATES	705			10			1			774	1		12	1		9		
INCORRECT ESCROW CHARGES																		
CONVEYANCE ISSUE																		
CONVEYANCE EXTENSION																		
RECORDS OF INSPECTIONS	517			1						565	1							
<b>FINDING AREAS IDENTIFIED</b>	<b>17</b>	<b>0</b>	<b>1</b>	<b>14</b>	<b>0</b>	<b>1</b>	<b>6</b>	<b>0</b>	<b>1</b>	<b>18</b>	<b>10</b>	<b>1</b>	<b>15</b>	<b>12</b>	<b>1</b>	<b>13</b>	<b>4</b>	<b>6</b>

HITS = REPORTED AS MISSING OR NEGATIVE; A = REPEAT FINDING; B = FINDING REPORTED IN HOC ASSESSEMENT REPORT

### Summary of Third Party Contractor File Review Inspection Results

DESCRIPTION	JULY									AUGUST									TOTAL		
	FIRST PRESTON			MCB			CITIWEST			FIRST PRESTON			MCB			CITIWEST			ALL		
	1153 FILES REVIEWED			183 FILES REVIEWED			120 FILES REVIEWED			1153 FILES REVIEWED			183 FILES REVIEWED			120 FILES REVIEWED			CONTRACTORS		
	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B	HITS	A	B
27011A RECEIVED				11	1		12	1	1	11			11	1		8	1		115	6	2
27011A DAMAGE CLAIMS				62	1								42	1					273	3	0
PART B REVIEW				130	1								108	1					354	3	0
INITIAL INSPECTION DATE	56			8	1					57	1		10	1					271	3	0
FILES COMPLETE AND ACCURATE				181			46			997			179	1		19	1		2676	2	0
DEED REQUEST	273			3						314			2	1					862	1	0
NOTATIONS TO TAX AUTHORITIES	259			179	1		12	1	1	346	1		178	1		5	1		2063	7	2
PRESERVATION AND PROTECTION	554	1		7	1		10			724	1					7	1		2403	7	0
HAZARDOUS CONDITIONS	2			21	1					4	1		21	1		1			90	4	0
HAZARDOUS MATERIALS REMOVED	2						2									2	1		8	1	0
EMERGENCY REPAIRS										6						1			22	0	0
MAJOR REPAIRS	62	1		1			18	1	1	104						12	1		272	4	2
APPRAISAL IN FILE	16	1		5	1		10			31	1		7	1		9	1		210	7	0
APPRAISAL DATE RECEIVED	18	1		21	1								8	1					118	5	0
APPRAISED WITHIN 10 DAYS	522	1	1	62	1	1	61	1	1	609	1	1	66	1	1	59	1	1	2384	9	11
DEFECTIVE PAINT CERTIFICATION	43	1		4	1		13	1	1	53	1		2	1		6	1		251	8	2
FILE DOCUMENTATION MAINTAINED							1						1			1	1		19	1	0
INSPECTION WITHIN 24 HOURS	389	1		55	1		52	1	1	438	1		67	1		40	1		2048	9	3
SUBSEQUENT INSPECTION DATES	738	1		5	1		5			865	1		9	1		2	1		3135	7	0
INCORRECT ESCROW CHARGES				1															1	0	0
CONVEYANCE ISSUE				1															1	0	0
CONVEYANCE EXTENSION				1															1	0	0
RECORDS OF INSPECTIONS	490	1		1						561	1		10	1					2145	4	0
<b>FINDING AREAS IDENTIFIED</b>	<b>14</b>	<b>9</b>	<b>1</b>	<b>20</b>	<b>13</b>	<b>1</b>	<b>12</b>	<b>6</b>	<b>6</b>	<b>15</b>	<b>10</b>	<b>1</b>	<b>16</b>	<b>15</b>	<b>1</b>	<b>14</b>	<b>12</b>	<b>1</b>	<b>174</b>	<b>91</b>	<b>22</b>

HITS = REPORTED AS MISSING OR NEGATIVE; A = REPEAT FINDING; B = FINDING REPORTED IN HOC ASSESSEMENT REPORT

**Nationwide Potential Duplicate Pass-through Payments Summary**

POST CODE	DESCRIPTION	Philadelphia HOC		Santa Ana HOC		Denver HOC	
		LINES	AMOUNT	LINES	AMOUNT	LINES	AMOUNT
AA	ARCHIVED CASE -DISBURS.	51	\$25,363.50				
AC	ALLOCATE EXPENSES	208	\$697,965.00			16	\$1,173.00
AD	ADVERTISING	6	\$18,000.00				
AM	M&M APPRAISAL REVIEW						
AO	DEFECTIVE PAINT/LBP REMOV	2	\$240.00				
AP	APPRAISAL	162	\$38,055.00				
BR	BOARD-UP/SECURE	139	\$12,059.00	17	\$2,220.00		
CD	CLEAN-UP & DEBRIS REMOVAL	139	\$23,039.45	9	\$1,890.31		
CF	CONDO FEES/HOA DUES	460	\$97,328.35	2,360	\$380,773.87	24	\$3,379.47
CL	CLOSING AGENT FEE	86	\$7,066.75	219	\$11,613.95	1	\$104.67
DF	DEFECTIVE PAINT/LBP REMOV	57	\$10,649.00				
EM	EARNEST MONEY - OVERWIRE	4	\$15,680.95	5	\$8,000.00	2	\$1,500.00
EV	EVICTIONS			54	\$164,027.00	2	\$112.00
FR	M&M FILE REVIEW						
GN	GENERAL REPAIRS	2	\$235.00	4	\$90.00		
IF	FEE INSPECTOR	966	\$60,630.31			7	\$1,445.00
JA	IMG SUB MECHANIC'S LIEN			1	\$1,320.00		
JB	IMG SUB PROP INSPECT FEE	11	\$3,450.00				
LC	REFUND KEY DEPOSIT			10	\$475.00	16	\$400.00
MI	FIRE REPORT	6	\$5,065.77				
MM	M&M MANAGER FEE			130	\$27,503.40		
MR	MISC MAJOR REPAIRS			1	\$1,364.00		
PE	SPEC PROPERTY REVIEW M&M	40	\$109,656.50	14	\$50,952.50		
PM	PROPERTY MANAGER FEE						
RB	REPURCHASE/BUYBACK EXPS						
SR	SYSTEM REPAIRS	3	\$1,340.00				
SS	SYSTEM CHECKS						
TL	TITLE EVIDENCE REVIEW	11	\$2,887.50				
TM	TERMITE TREATMENT	3	\$1,925.80	2	\$1,645.00	1	\$350.00
TR	TERMITE INSPECTION						
TX	UNCOLLECTED TX AT CLSG	1	\$437.41	1	\$220.38	3	\$3,732.05
UT	UTILITIES/FUEL OIL	572	\$54,093.95	1,866	\$38,908.65	113	\$1,850.73
VR	VOUCHER REVIEW - ALLOCATE						
WN	WINTERIZING	16	\$719.40	4	\$356.00		
WT	WATER	11	\$2,456.92	17	\$417.83		
YR	YARD MAINTENANCE			95	\$2,175.00		
	<b>TOTALS</b>	<b>2,956</b>	<b>\$1,188,345.56</b>	<b>4,809</b>	<b>\$693,952.89</b>	<b>185</b>	<b>\$14,046.92</b>

**Nationwide Potential Duplicate Pass-through Payments Summary**

POST CODE	DESCRIPTION	Atlanta HOC		Headquarters		Totals	
		LINES	AMOUNT	LINES	AMOUNT	LINES	AMOUNT
AA	ARCHIVED CASE -DISBURS.					51	\$25,363.50
AC	ALLOCATE EXPENSES	187	\$95,080.00			411	\$794,218.00
AD	ADVERTISING	6	\$79,200.00			12	\$97,200.00
AM	M&M APPRAISAL REVIEW	54	\$540.00			54	\$540.00
AO	DEFECTIVE PAINT/LBP REMOV					2	\$240.00
AP	APPRAISAL	408	\$116,353.86			570	\$154,408.86
BR	BOARD-UP/SECURE	38	\$4,787.50			194	\$19,066.50
CD	CLEAN-UP & DEBRIS REMOVAL	248	\$44,081.08			396	\$69,010.84
CF	CONDO FEES/HOA DUES	258	\$29,053.24			3,102	\$510,534.93
CL	CLOSING AGENT FEE	270	\$13,709.22			576	\$32,494.59
DF	DEFECTIVE PAINT/LBP REMOV	39	\$17,660.50			96	\$28,309.50
EM	EARNEST MONEY - OVERWIRE	1	\$1,048.92			12	\$26,229.87
EV	EVICTIONS					56	\$164,139.00
FR	M&M FILE REVIEW			6	\$680,616.00	6	\$680,616.00
GN	GENERAL REPAIRS	21	\$2,583.00			27	\$2,908.00
IF	FEE INSPECTOR	2	\$120.00			975	\$62,195.31
JA	IMG SUB MECHANIC'S LIEN	1	\$25.00			2	\$1,345.00
JB	IMG SUB PROP INSPECT FEE	2	\$570.00			13	\$4,020.00
LC	REFUND KEY DEPOSIT					26	\$875.00
MI	FIRE REPORT	1	\$6,500.00			7	\$11,565.77
MM	M&M MANAGER FEE					130	\$27,503.40
MR	MISC MAJOR REPAIRS					1	\$1,364.00
PE	SPEC PROPERTY REVIEW M&M	1	\$19,946.01			55	\$180,555.01
PM	PROPERTY MANAGER FEE	475	\$96,220.00			475	\$96,220.00
RB	REPURCHASE/BUYBACK EXPS	28	\$2,100.00			28	\$2,100.00
SR	SYSTEM REPAIRS	2	\$175.00			5	\$1,515.00
SS	SYSTEM CHECKS	116	\$15,525.00			116	\$15,525.00
TL	TITLE EVIDENCE REVIEW	1	\$125.00			12	\$3,012.50
TM	TERMITE TREATMENT	69	\$30,060.00			75	\$33,980.80
TR	TERMITE INSPECTION	11	\$555.00			11	\$555.00
TX	UNCOLLECTED TX AT CLSG					5	\$4,389.84
UT	UTILITIES/FUEL OIL	316	\$6,945.81			2,867	\$101,799.14
VR	VOUCHER REVIEW - ALLOCATE	1	\$14,132.49			1	\$14,132.49
WN	WINTERIZING	157	\$15,242.75			177	\$16,318.15
WT	WATER					28	\$2,874.75
YR	YARD MAINTENANCE	87	\$2,610.00			182	\$4,785.00
	<b>TOTALS</b>	<b>2,800</b>	<b>\$614,949.38</b>	<b>6</b>	<b>\$680,616.00</b>	<b>10,756</b>	<b>\$3,191,910.75</b>

**Auditee Comments**



**U.S. Department of Housing and Urban Development**

Homeownership Center  
The Wanamaker Building  
100 Penn Square East  
Philadelphia, Pennsylvania 19107-3389

**MAY 23 2001**

TO: Daniel G. Temme, District Inspector General for Audit, Mid-Atlantic, 3AGA

FROM: Engram A. Lloyd, Director, Philadelphia Homeownership Center  
3AHH

SUBJECT: Comments on Draft Audit Memorandum dated May 3, 2001  
Philadelphia Homeownership Center  
Single Family Disposition Activities

We have reviewed the subject draft audit report and agree with the findings and proposed recommendations. We propose the attached management decision(s) for your concurrence.

cc:  
Cliff Cole, 3BGA

*Visit our web page at [http://www.hud.gov/fha/sfh/talk/addr\\_phi.html](http://www.hud.gov/fha/sfh/talk/addr_phi.html)*

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