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OFFICE OF INSPECTOR GENERAL FOR AUDIT

Audit Memorandum
No. 2001-DE-0801

September 28, 2001

MEMORANDUM FOR: Ronald C. Bailey, Director, Denver Homeownership Center, 8AHH

FROM: Robert Gwin, District Inspector General for Audit, 8AGA

SUBJECT: Denver Homeownership Center
Review, Approval and Monitoring of Nonprofit Organizations' Participation in FHA Single Family Insurance Programs

INTRODUCTION

We have completed an audit of the Denver Homeownership Center's review, approval, and monitoring processes of Nonprofit Organizations' participation in FHA Single Family Insurance Programs. The objectives of the audit were to determine whether:

- HUD's existing policies, procedures and guidelines (those implemented in response to Mortgagee Letter 00-8) are sufficient to ensure nonprofit agencies, HUD approves for participation in its single family insurance programs, are legitimate nonprofits not acting under the influence of outside parties such as realtors, consultants, investors, etc.; have Affordable Housing Plans which meet HUD requirements; and have sufficient previous experience to allow them to carry out their programs.

- HUD's procedures for monitoring the activities of approved nonprofit agencies are adequate to determine if the agencies are carrying out their housing activities in accordance with their housing assistance plan in a fiscally sound manner and whether the benefits of discounts received on the purchase of HUD homes are being passed on to low- and moderate-income homebuyers.

- HUD has procedures in place to take quick and effective action against those it identifies as having abused the program and if so whether these actions are actually taken. Such action would include removal from the program, limited denial of participation, debarment, and/or other administrative actions.

- HUD has established revitalization areas in accordance with outstanding guidelines and whether it has adequate policies in place to ensure that applicable 30 percent discount home sales to nonprofit agencies are in eligible areas.

To accomplish our objectives, we reviewed the Denver Homeownership Center's Program Support Division's and Real Estate Owned Division's files and records. We interviewed various HUD officials of these two divisions. In addition, we conducted site reviews of two approved nonprofit entities that were participating in HUD's FHA Single Family Insurance Programs. These two nonprofits were Brothers Redevelopment, Inc., located in Denver, Colorado, and Community Housing Fund, located in Dallas, Texas. We reviewed various accounting records and files of these two entities as well as applicable organizations and companies doing business with the two nonprofits. We also interviewed low- and moderate-income purchasers of discounted properties sold by nonprofit agencies and visited and inspected some of the sold properties.

Our audit period was January 1, 1998 through January 31, 2001; however the audit period was expanded to include the most current data available while performing the site work. Therefore, where applicable the audit period was expanded to include current data through June 30, 2001. We conducted fieldwork from March through June 2001. The results of the site work accomplished at two nonprofit entities were discussed with officials from these organizations during our site review. The draft audit finding was presented to the Denver Homeownership Center on August 28, 2001 for their verbal comments. The draft audit memorandum was presented to the Denver Homeownership Center's staff for their review and written comment on September 12, 2001. The Director of the Denver Homeownership Center determined that an exit conference was not necessary since they basically concurred with the findings and recommendations and the results of the audit had been communicated on a continual basis during the review. Their written response is included in Appendix A.

The results of our review of the two nonprofit organizations are presented in separate audit reports.

Our review was conducted in accordance with generally accepted government auditing standards.

BACKGROUND

In an attempt to provide increased affordable housing opportunities to low and moderate-income homebuyers, HUD has encouraged nonprofit organizations to participate in HUD's FHA Single Family Insurance Programs. Nonprofit and government organizations can participate in various activities of the HUD FHA Single Family Insurance Programs. These activities include:

- Mortgagors – The approved organizations can purchase properties from HUD or any other party and obtain FHA insured mortgages.

- The HUD Homes Program (Real Estate Owned Discount Sales Program) – Approved nonprofit and government organizations can purchase HUD owned properties at discounts ranging from 10 to 50 percent off the as-is appraised value of the property(s).

- Secondary Financing – Nonprofit and governmental organizations can obtain HUD approval to provide mortgagors (purchasing properties using FHA-insured financing) secondary financing in the form of second mortgages or "soft" second mortgages.

- Downpayment Assistance – Nonprofit agencies can provide a gift to mortgagors for all or part of their downpayment and closing costs. With the issuance of Mortgagee Letter 00-8, HUD approval is no longer required for this part of the program.

One of the principle documents used to determine whether a nonprofit organization will be approved to participate in HUD's discount sales program as an approved mortgagor, is its' Affordable Housing Program. Among other things, this program is to describe the nonprofit's purpose for participating in FHA programs, how low- and moderate-income persons will benefit from the program, and how the nonprofit will pass along to low income persons any savings received from the discounted purchase of a HUD-owned property. Each of the four HUD Homeownership Centers is to review and approve nonprofits and the Affordable Housing Programs for their applicable jurisdictions.

Every two years, nonprofit entities are required to re-certify their organizations and their Affordable Housing Programs. The recertification is similar to the initial application, but also includes a detailed description of the activities undertaken during the previous two years. Essentially, the nonprofit organizations are to use this recertification to demonstrate whether they have created affordable housing opportunities in a fiscally responsible way.

Annually, nonprofits who have purchased HUD homes at a 30 percent discount are to provide a report to the Homeownership Center Director providing detailed information on their program accomplishments over the past calendar year. This information is to include detailed information on each property it purchased at a 30 percent discount and subsequently resold. Nonprofits purchasing properties at a 15 percent or less discount are exempt from this reporting requirement.

The responsibility for the review, approval, and monitoring of nonprofit agencies and their participation in FHA Single Family Insurance Programs, within the Homeownership Centers, was transferred from the Real Estate Owned Division to the Program Support Division in February 2000. Shortly after this transfer of responsibility, Mortgagee Letter 00-8 was published on March 3, 2000. This letter required all nonprofits to resubmit their recertification packages to participate in the HUD program within 45 days from the date of issuance of the letter. The Denver Homeownership Centers staff received approximately 160 recertification packages for review. They reviewed and approved approximately 100 of the nonprofit agencies and disapproved approximately 60 of the nonprofit agencies.

RESULTS OF REVIEW

We reviewed the Denver Homeownership Center's procedures and controls over the review, approval, and monitoring processes of nonprofit organizations participation in FHA Single Family Insurance Programs. The Denver Homeownership Center has established various procedures and controls to carryout its' management and oversight of nonprofits and their Affordable Housing Programs. We found that the Denver Homeownership Center needs to modify these procedures and controls in order to improve its oversight activities of the nonprofits. These areas are discussed in the following finding:

FINDING - Improvement Needed In The Oversight of Nonprofit Entities

The Denver Homeownership Center through its Program Support Division has the responsibility for ensuring that nonprofit entities participating in HUD's FHA Single Family Insurance Programs are eligible and carryout their activities in conformity within established requirements. Our review of the Denver Homeownership Center's procedures and controls over the review, approval, and monitoring processes of nonprofit agencies' participation in FHA Single Family Insurance Programs showed where improvements are needed in three areas:

- Previously approved nonprofit agencies were granted approval to participate in FHA's Single Family Insurance Programs when their recertification packages did not fully comply with the requirements of Mortgagee Letter 00-8;
- New nonprofit agencies were granted approval to participate in HUD's program when their certification packages did not fully comply with the requirements of Mortgagee Letter 00-8; and
- The required annual reports from the nonprofit agencies that had purchased 30 percent discounted properties during the preceding year did not include data on all acquired properties or were not being received.

By making the needed changes in program oversight, the Program Support Division will be better able to ensure that its nonprofit entities are properly authorized and are performing their approved Affordable Housing Programs within established HUD provisions and requirements.

HUD Requirements Mortgagee Letter 00-8 stated that in an attempt to verify that all nonprofit agencies were meeting and furthering the goal of the Department to create homeownership opportunities for low- and moderate-income persons, all approved nonprofit agencies had to submit a complete recertification package to the applicable Homeownership Center no later than April 17, 2000. Nonprofit agencies were to use the guidelines in Mortgagee Letter 96-52 for details regarding successful elements of an affordable housing plan. Also this mortgagee letter states the requirement that nonprofit agencies that purchase HUD homes at the 30 percent discount level must submit an annual report, along with supporting documentation, to the applicable Homeownership Center. This information was to detail their program accomplishments over the previous calendar year by February 1 of the following year. The Homeownership Center was to review these accomplishments and supporting documentation to determine, among other things, that substantial benefits were passed on to the homeowner as a result of the nonprofit agency receiving a 30 percent discount on the property. Failure to pass on adequate savings to the ultimate homeowner could result in removal from the approved list of nonprofit entities.

Mortgagee Letter 96-52 states that in order for a nonprofit agency to receive the same insured financing percentage as owner-occupants, the nonprofit must be a tax-exempt organization, have a voluntary board whose members do not personally benefit from the affordable housing program, and have two years experience as a housing provider. A successful affordable housing plan is to incorporate these elements:

- The nonprofit should pre-qualify the potential homebuyers;

- The principle, interest, taxes, and insurance for the property should remain in the affordable range for potential homebuyers; and

- Beneficiaries of the affordable housing program may not be members of its board, employees, or others with an identity of interest to the nonprofit.

HUD requires the management of approved nonprofits to act on their own behalf and not be under the influence, control, or direction of any outside party seeking to derive profit or gain from the proposed project, such as landowners, real estate brokers, contractors, builders, lenders, or consultants.

Previously Participating Nonprofit Recertification Package Discrepancies We reviewed the recertification packages submitted to HUD in accordance with Mortgagee Letter 00-8 for two previously participating nonprofits. These two entities were Community Housing Fund and Brothers Redevelopment, Inc., both of which were two of the largest nonprofit agencies in the Denver Homeownership Center's area of responsibility. Both of these nonprofits had deficiencies in their recertification packages that should have been identified in the package review by the Program Support Division. These are discussed below:

Community Housing Fund The recertification package for Community Housing Fund did not identify any identity of interest issues between the nonprofit and its' rehabilitation contractor. We utilized a computer software program that was available to the Program Support Staff and identified indicators that an identity of interest issue possibly exists between the nonprofit and its' rehabilitation contractor. The identities of interest issues were confirmed by on-site audit work. The President of the nonprofit had more than an arms length relationship with the rehabilitation contractor.

Data obtained from the computer software package Choice Point, which owns Auto Track, and from a search of Internet public records identified these relationships between the two parties:

- The President of Community Housing showed as a Director of Ranscott 12th Hialeah Corp., which was deactivated in 1990 and of The Ranscott Group, Inc., which was deactivated in 1993. These two companies appear to be the forerunners of Ranscott Construction Company, the current rehabilitation contractor for Community Housing Fund.

- The President of Community Housing and several of the owners of Ranscott Construction are using the same mailing address.

- One of the owners of Ranscott Construction is shown on the Articles of Incorporation for Community Housing Fund as one of the original Directors.

These identity of interest issues could have been identified by HUD had the computer software programs been used as part of the review process of the recertifications. Had these possible identity of interest issues been disclosed, the Denver Homeowner Center would have been able to obtain clarifying information from the recertifying nonprofit before the recertification package was approved.

Brothers Redevelopment, Inc. Information contained in the recertification package for Brothers Redevelopment, should have raised some questions as to whether the nonprofit should have been approved for further participation in HUD's FHA Single Family Insurance Programs, without further investigation and clarification. These items were noted in Brothers Redevelopment's recertification package:

- No copies of prior participation approval letters previously provided by a HUD office or the Denver Homeownership Center to Brothers Redevelopment in the recertification package as required.

- A list containing the name, address and contact of any lending institution or bank which has provided financing in the past, or which would be financing future property acquisitions, was not contained in the package as required.

- A statement was made in Brothers Redevelopment's recertification package as part of its Affordable Housing Program that indicated that benefits from the purchase of discounted HUD properties did not need to be passed on to the low- and moderate-income homebuyers.

The first two items were part of the requirements to be presented in the recertification package. However these were overlooked as part of the review process. The third item indicates that Brothers Redevelopment's Affordable Housing Program was in direct conflict with HUD's stated objectives to provide housing opportunities to low- and moderate-income homebuyers and to pass on the savings from the purchase of discounted properties to the low- and moderate-income homebuyers. The statement also indicates that potential buyers of Brothers Redevelopment's discounted properties might not meet the requirements of being low- and moderate-income purchasers.

These items indicate that the recertification package for Brothers Redevelopment should not have been approved without further information and clarification being obtained from the nonprofit.

New Participating Nonprofit Certification Package Discrepancies In our review of two of three initially certified packages for newly approved non-profits, we identified areas that could have been identified by the Homeownership Center. Had the information been disclosed, the Homeownership Center would have been able to address the concerns and ensure that the new nonprofits were properly approved to participate in HUD's FHA Single Family Insurance Programs. These two nonprofits were Texas Fathers for Equal Rights and Grand Isle Area Housing Corp. These are discussed below:

Texas Fathers for Equal Rights The certification package submitted to HUD did not identify any identity of interest issues between the nonprofit and its' rehabilitation contractor. We conducted a search using a computer software program available to the Homeownership Center's review staff and found an identity of interest concern between the Director of the nonprofit, one of its Board members, and a local construction company.

The Director and a Board member are married and they jointly own a construction company called DFW Rehab. This construction company has the ability to do rehabilitation work on the nonprofit's single-family properties. The Director stated in her resume, concerning her construction company, that "*DFW Rehab is working under a non-exclusive agreement with Fathers for Equal Rights to manage and perform the renovation for Fathers for Equal Rights' Affordable Housing Program*." After this was brought to the Program Support Division's attention, they had the nonprofit submit a letter stating that the nonprofit would not do business with DFW Rehab.

Grand Isle Area Housing Corp. This new nonprofit made a statement in their Affordable Housing Plan that was submitted as part of their certification package to HUD that "*the client will still need to purchase the home for the maximum loan they had been prequalified for, any savings the GIAHC* [Grand Isle Area Housing Corp.] *may realize from the discounted purchase price will be put back into program funds to allow more persons to be assisted.*" This statement of the nonprofit indicates their Affordable Housing Program will be conducted in a manner that is in direct conflict with HUD's objective of the program to provide housing opportunities to low- and moderate-income buyers and to pass on the savings from the purchase of discounted properties to the homebuyer.

The Homeownership Center's review of this nonprofit's Affordable Housing Program did not question the apparent conflict between the nonprofit's intended program operation and HUD's program requirements. Had this been identified, the nonprofit should have been required to modify its Affordable Housing Program before it was approved by the Homeownership Center.

In addition to reviewing the participation packages for nonprofits, we also reviewed the participation package of a governmental entity, Minneapolis Community Development, and found the package did not contain all the necessary documentation as required by HUD. Details are:

Minneapolis Community Development The certification package for this government agency did not contain sufficient evidence that the entity met the required criteria to be considered an "instrumentality of government". Under the provisions of HUD Handbook 4155.1, Rev-4, Chapter 1, Section 1, Paragraph 1-5. B, the agency must present evidence from its legal counsel that the entity has the legal authority and capacity to become a mortgagor, the local government is not in bankruptcy, and the entity had no prohibition to prevent a lender from obtaining a deficiency judgment on HUD's behalf in the event of property foreclosure or deed-in-lieu foreclosure.

The application letter from the government entity stated that they were a public body, corporate, and politic of the State of Minnesota and that a copy of their By-Laws was enclosed in their certification package. However, no evidence was presented in the package of what designated them as an "instrumentality of government" such as a letter from their legal counsel. In addition, a copy of the By-Laws was not contained in the package as indicated.

With the needed information not being included in the governmental entity's certification package, HUD lacked supporting evidence to substantiate the entity had the required legal authority and was eligible to participate in HUD FHA Single Family Insurance Programs. The certification package should have been modified by the governmental entity before HUD approved the entity and its' certification package.

Nonprofits' Annual Reports Discrepancies Under HUD's requirements, those nonprofits that purchase HUD properties at a discount of 30 percent or more are to file annual reports with HUD detailing information on each property. For those nonprofits we reviewed, we compared data on discounted properties sold by HUD using HUD's property sales database with the purchased property information contained in the nonprofits' annual report. This comparison showed that three nonprofits did not report all of the 30 percent discounted property purchases. The three nonprofits were Community Housing Fund, Brothers Redevelopment, Inc., and Minneapolis Community Development. Information on the omitted properties is discussed below:

Community Housing Fund Community Housing Fund omitted from its annual report a property located on Newcombe Drive in Dallas. Further information on this property obtained from computer databases available to the HUD review staff indicated that the property was sold to a possible investor who owns several other properties. The sale of this property to an investor would not be in conformity with HUD requirements. On-site audit work confirmed that the property had been sold to an investor.

Brothers Redevelopment, Inc. Brothers Redevelopment, Inc. did not include a 30 percent discounted property located on 47th Avenue in Denver. Subsequent information furnished by the nonprofit to the Denver Homeownership Center showed that this property was financed with an unusually high interest rate of 19.5 percent and the profits realized from the sale of the thirty percent discount property were distributed among the nonprofit, its' contract developer, and its' primary lender. This indicated that the nonprofit was not passing on benefits realized from the purchase of the 30 percent discounted properties to its low- and moderate-income homebuyer as intended by HUD under the program.

Minneapolis Community Development This governmental entity purchased three 30 percent discount properties from HUD in 2000 but no annual report was submitted to HUD as required.

Approved Nonprofit Entities May Be Ineligible Program Participants These deficiencies discussed above illustrate that the certification or recertification packages should not have been approved. Information in the packages and/or independent information obtained from available computer software programs raised questions about whether a nonprofit had been or intended to carryout its' program within HUD program requirements. Subsequent to the approvals, HUD has obtained information that some of the nonprofits were indeed not properly administering their Affordable Housing Program as required by HUD. This can be shown by the following two examples.

Community Housing Fund The recertification package for Community Housing Fund did not identify any identity of interest issues between the nonprofit and its' rehabilitation contractor. Information obtained from computer software programs available to HUD staff showed an apparent identity of interest issue. Further computer software searches as well as a review of HUD's Single Family computer data systems showed that some discounted properties acquired by Community Housing Fund were sold to apparent investors. Both of these activities are prohibited under HUD's program. Based upon further information obtained by the Denver Homeownership Center staff and information stemming from our on-site review of the nonprofit's activities, HUD has suspended the nonprofit from participating in the program.

Brothers Redevelopment, Inc. Brothers Redevelopment, Inc. indicated in their Affordable Housing Plan that profits realized from the purchase of discounted properties did not need to be passed on to the ultimate low- and moderate-income homebuyer. Subsequent to HUD approving Brothers Redevelopment, Inc. as a program participant, information obtained by HUD disclosed that the nonprofit has not administered its Affordable Housing Program within HUD requirements. Based on additional information received by the Denver Homeownership Center as part of their on-site program review and our detailed site audit at the nonprofit, HUD suspended the nonprofit.

Brothers Redevelopment, Inc. has allowed an independent contract developer to administer all major phases of its Affordable Housing Program in order to receive the maximum possible profit from the program. Profits realized under their program were distributed among the nonprofit, its' contract developer and the contract developer's identity of interest program lender. The real impact was that benefits being realized from the purchase of the discounted HUD properties were not passed on to the low- and moderate-income homebuyer as intended by the HUD program.

Statements in the recertification packages and/or other information available to HUD for these two nonprofit organizations indicate that the entities were possibly going to deviate from HUD requirements in carrying out their Affordable Housing Programs. Once approved, the nonprofit organizations did administer their programs for their own best interest and not within the parameters set by HUD. Furthermore, benefits from acquiring discounted HUD homes were not passed on to low- and moderate-income homebuyers.

HUD's Review Procedures Can Be Improved In February 2000, the responsibility for reviewing, approving, and monitoring of nonprofit organizations in HUD's FHA Single Family Insurance Programs was transferred from the Real Estate Owned Division to the Program Support Division within the Denver Homeownership Center. In March 2000, HUD issued Mortgagee Letter 00-8 that required all previously approved nonprofit organizations as well as any new nonprofit organizations to submit within 45 days new certification packages to HUD for review and approval for the HUD program. HUD with newly assigned review staff had to complete the review of approximately 160 certification packages in a 90-day period.

According to Homeownership Center officials, this situation resulted in a very heavy workload that had to be conducted in a very limited timeframe. As a result, some areas of the certification package reviews may have been deficient. The Homeownership Center staff did a good job of reviewing the certification packages considering the fact that the reviews had to be completed in a short time period and that the reviewing staff had received very limited guidance on how to carryout their review functions. The Program Support Division staff were not given written instructions on how to accomplish the review, approval and monitoring processes other then the guidelines contained in the various Mortgagee Letters. Senior Program Support Division personnel from the Denver Homeownership Center accomplished the training and writing of instructions, on how to accomplish the review, approval and monitoring processes, while their staff worked their way through the recertification process.

While the Denver Homeownership Center has done a good job of carrying out their review responsibilities within the limited time frames and guidance provided, improvement can be made in four areas. These four areas are:

First, under HUD guidelines, all recertification packages must be submitted to HUD every two years for HUD's review and approval. The next cycle will be in April 2002. All of these packages must be reviewed within a limited time frame. Consequently, the Homeownership Center staff may not have sufficient time by which they can conduct a more comprehensive review of each nonprofit package. This situation could be improved if the receipt and review of the packages were staggered throughout the year rather than at one point in time. In our opinion, this would allow the Homeownership Center staff to spread their review process over the year and thereby allow them more time to review each package. Obviously consideration needs to be given by the Homeownership Center in adjusting the workload throughout the year.

Second, the Homeownership Center has not utilized the various available computer software programs in gathering information to evaluate and validate the information and data that is contained in the certification packages. As discussed above, data that was obtained from these computer systems identified facts that were not clearly disclosed in the certification packages and related affordable housing plans. Clarification would have aided HUD in ensuring that the nonprofits were to operate their programs within the parameters set by HUD. Also the additional facts may have led HUD to conclude that the certification/recertification packages and the nonprofit entity not be approved.

The Homeownership Center could also use its' various computer data systems to verify that the nonprofits are properly reporting information on all of the 30 percent discounted properties acquired from HUD.

Third, the Homeownership Center used a checklist to aid the staff in reviewing the certification packages from the nonprofits. The checklist is structured in a way that any checklist item that is marked with a negative response would need additional follow up and/or corrective action. We identified some items in the checklist that indicated that follow up and corrective action was needed but, for some reason, was not done. In our opinion, clarification and guidance needs to be provided to the review staff to ensure that any questionable items in the package review are pursued and resolved before the package is approved. Accordingly, such resolutions would need to be documented.

Fourth, the Homeownership Center has not implemented a process to evaluate whether or not the nonprofits are passing on any benefits from the purchase of the 30 percent discounted HUD properties to the ultimate homebuyer. As part of the review process of the annual reports or recertification packages from the nonprofits, an evaluation of the nonprofit submitted data could be performed to ascertain that benefits from discounted properties are being passed on to the homebuyer. If a determination cannot be readily determined, supplemental information on selected sample properties might need to be obtained from the nonprofit. This process would enable the review staff to evaluate whether any realized benefits are being passed on to the homebuyer or not.

Had a similar process been in place when the recertification packages for Community Housing Fund and Brothers Redevelopment, Inc. were reviewed, a determination possibly could have been made that profits from discounted properties were indeed not being granted to the property purchaser. When HUD did ask Brothers Redevelopment, Inc. for information on the one discounted property that was not reported in their recertification package, the supplied data clearly suggested that no program benefit was being given to the purchaser. Subsequent onsite review by the Denver Homeownership Center staff as well as by our review clearly substantiated this fact. As a result, HUD has suspended the nonprofit.

When items of concern and/or deficiencies we identified as part of our audit were presented to the Denver Homeownership Center staff, they initiated immediately steps to clarify and/or correct the items of concern and/or deficiencies. This has included the suspension of nonprofits that were identified as not conducting their Affordable Housing Program within HUD requirements. The Denver Homeownership Center has taken positive steps to improve their review, approval and monitoring oversight of its' nonprofits. By modifying its' review and approval process, the Denver Homeownership Center will be better able to ensure that the approved nonprofits are properly carrying out their programs and that benefits from acquired HUD discounted properties are being passed on to the purchasing low- and moderate-income homebuyers.

Denver Homeownership Response

The Denver Homeownership Center's written reply to the draft audit memorandum provided information and explanations to the various sections delineated in the audit finding. In some cases, the Denver Homeownership Center did not entirely agree with the position being taken in the finding. However, the Denver Homeownership Center has initiated actions that address the issues presented in the finding. In addition, two Mortgagee Letters are being drafted and/or being processed for issuance that will provide guidance and clarification on the HUD FHA Single Family Insurance Programs.

Recommendations

We recommend that the Denver Homeownership Center:

1A. Devise a plan to stagger the review process for all recertifications packages that are going to be coming due in April 2002.

OIG Comment: The Denver Homeownership Center stated in their written response that nationally, Single Family Housing is aware of the logjam of work that is submitted during a short time period. Headquarters, in conjunction with the four Homeownership Centers, is working on a plan to implement staggering approval dates in order to spread this work out in a more manageable manner. Accordingly, no further action is considered necessary and this recommendation is being considered closed.

1B. Implement procedures to utilize various available computer software programs such as Auto Track, as part of the Homeownership Center's review of information that is presented in the certification/recertification packages and related affordable housing plans from the nonprofit entities. The procedures would need to include providing appropriate training to the staff on the use of such computer software programs. This will also include the use of HUD Single Family computer data to verify that all acquired 30 percent discounted properties are correctly reported by the nonprofits in their annual report.

OIG Comment: The Denver Homeownership Center stated in their written response that the Program Support Staff are now aware of these programs and the information they can provide and are utilizing them in new applications and review of existing agencies. The Program Staff is also now obtaining SAMS reports on a monthly basis of the discounted sales to nonprofit and government agencies and these reports will be used to compare reports received against actual sales. Therefore, no additional action is considered necessary and this recommendation is being considered closed.

1C. Clarify procedures on the use of the certification/recertification package checklist and what actions and documentation is needed when discrepancies are noted in the review of nonprofit certification/recertification packages and applicable Affordable Housing Programs.

1D. Formulate a process to evaluate information submitted by the nonprofit organizations on whether benefits from 30 percent discounted properties are being granted to the low- and moderate-income purchaser.

Recommendations 1C and 1D will be controlled under the Departmental Automated Audit Management System. Within 60 days please furnish to this office, for each recommendation in this report, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered not necessary. Also, please furnish us copies of any correspondence or directives issued because of the audit.

We appreciate the courtesies and assistance extended by the personnel of the Denver Homeownership Center. The personnel of the Program Support Division and the Real Estate Owned Division all appeared to be very professional and conscientious and were very receptive to our suggestions. Should you have any questions please contact Ernest Kite, Assistant District Inspector General for Audit, at (303) 672-5452.

Appendix A

Auditee's Comments:

U.S. DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT
HOMEOWNERSHIP CENTER
633 17TH ST.
DENVER, COLORADO 80202-3690

September 18, 2001

MEMORANDUM FOR: Robert Gwin, District Inspector General for Audit, ~~8AGA~~

FROM: Ronald C. Bailey, Director, Denver Homeownership Center

SUBJECT: Response to Review – Denver Homeownership Center Non-Profit Process

Attached is our response to your draft report on the Denver Homeownership Center and our procedures regarding the review, approval and monitoring of nonprofit organizations participation in FHA Single Family Insurance Programs.

We understand that these comments will be added to your final report and may have an effect on the final report as to findings and recommendations. If you should have any questions with regard to these comments, please speak with Dawn Davis or Jane Hall of my staff.

Response to OIG Draft Audit Report

Finding – Improvement needed in the Oversight of Nonprofit Entities

The draft report identified *three* areas where improvement is needed by the Program Support Division of the Denver Homeownership Center in their approval and review of nonprofits participating in our programs. Following is our response to the three areas identified by the OIG:

1. **Previously approved nonprofit agencies were granted approval to participate in FHA's Single Family Insurance Programs when their recertification packages did not fully comply with the requirements of Mortgagee Letter 00-08: More specifically referring to Community Housing Fund and Brothers Redevelopment Inc.**

Community Housing Fund:

- Possible identity of Interest: Previous to early 2001, the Auto Track System was being tested and utilized on a limited basis within other HUD offices (not the HOC). The Program Support Division was unaware of the Auto Track System and its availability until early in 2001. Therefore, during the recertification process driven by Mortgagee Letter 00-08, Program Support staff did not have access to Auto Track to perform identity of interest checks. Not until July 2001 did the Program Support staff receive training and access to Auto Track that has now been converted to Choice Point. We are utilizing this system to perform identity of interest checks on new nonprofit applications as well as in our review process of existing nonprofits.

Brothers Redevelopment:

- No previous approval letter was in the file for recertification. Because this nonprofit agency was in Denver and the Denver office and Program Support staffs were very familiar with this agency and their prior approval status, the determination was made to approve them without of copy of their previous approval letter in the file. BRI had a long history with several offices within the Denver HUD office.
- There was no list of lending institutions or banks providing financing to BRI. There was, however, reference to BRI's financial capacity, HUD funding, and fund raising activities. It was assumed they were financially capable of financing this program with their own resources as they had done business with many HUD offices throughout the years
- The statement made by BRI that there is no requirement to pass on the benefit of the discount is taken out of context. During the time of BRI's approval, there was no HUD requirement for any 10% discount sale savings to be directly passed to a specific affordable homebuyer. BRI does state that they had no requirement to

pass on a benefit but then went on to state that the homes would be sold within the affordable housing range and that the sales would be made to low and moderate income families. BRI did buy a low number of 30% discounted properties and was expected to adhere to the 110% of net development on these, and if calculated properly, would have insured that a savings be passed on to the purchaser.

2. New nonprofit agencies were granted approval to participate in HUD's program when their certification packages did not fully comply with the requirements of Mortgagee Letter 00-08.

Fathers for Equal Rights

- Identity of interest. As discussed above in this response, the Auto Track system was being tested at the time of approval and the Program Support staff was unaware of its capabilities to assist with uncovering identify of interests with nonprofit approval and recertification. Staff is now aware of Choice Point and its capabilities and will utilize it with future approvals and reviews.

Grand Isle Area Housing Corp.

- Their statement that any savings realized would be put back into program funds to assist more persons was not out of the realm of what would be allowed. In Mortgagee Letter 00-08, Question 4 in the format for an Affordable Housing Plan asks: How will your program be designed to pass along to low income persons any savings your agency may receive from discounted sales? It doesn't specifically say that savings from *that* particular sale needs to be passed along to *that* particular borrower. Putting money back into the program to assist more homeowners is not disallowed. Their overall program was taken into consideration. The second part to that question asks: How will you ensure that payments are affordable? By qualifying their purchaser through an FHA lender, the purchaser would be qualified based on the 29/41% ratios that FHA determines is affordable and reasonable. That was acceptable.

Minneapolis Community Development

- This agency had previously participated in providing secondary financing as an instrumentality of Government. During recertification, only nonprofits were required to recertify. Because of their previous determination as an "instrumentality of Government" they were not required to be reapproved. We did, however, provide them with an approval letter for their files when asked for by lenders utilizing their secondary financing. We have since obtained documentation for their file that provides the ordinance where the Minneapolis City Counsel created them as a "body corporate and politic which shall be a governmental subdivision of the state." They meet criterion A and B3 in

Mortgagee Letter 94-2 which provides secondary financing requirements. No letter from their legal counsel was necessary.

3. **The required annual reports from the nonprofit agencies that had purchased 30 percent discounted properties during the preceding year did not include data on all acquired properties or were not being received.**

Program Support staff was not responsible for analyzing the 30% discounted sales reports until after the issuance of Mortgagee Letter 00-08 in March 2000. Program Support is now obtaining year end reports and acquiring monthly reports as well and will be preparing the next year end reports for comparison against the reported information in the SAMS reports of actual sales.

Recommendations by OIG

1A. Devise a plan to stagger the review process for all recertification packages that are going to be coming due in April 2002.

- Nationally, Single Family Housing is aware of the logjam of work that is submitted during a short time period. Headquarters, in conjunction with the four Homeownership Centers, is working on a plan to implement staggering approval dates in order to spread this work out in a more manageable manner.

1B. Implement procedures to utilize various available computer software programs such as Auto Track or Choice point when reviewing applications.

- As discussed previously, the Program Support staff are now aware of these programs and the information they can provide and are utilizing them in new applications and review of existing agencies. Program Support is also now obtaining SAMS reports on a monthly basis of the discounted sales to nonprofit and government agencies and these reports will be used to compare reports received against actual sales.

1C. Clarify procedures on the use of the certification/recertification package checklist.

- The checklist has recently been revised and is intended to list items which will be required to be submitted from a nonprofit in their application. A Mortgagee letter is in clearance at this time, clarifying what is required and provides a copy of the checklist. Staff will be trained to assure that information submitted is in compliance with what is required by the checklist.

1D. Formulate a process to evaluate information submitted by the nonprofit organizations on whether benefits from 30% discounted properties are being granted to the low- and moderate-income purchaser.

- Two new Mortgagee Letters are currently in clearance that will clarify what is required/allowed in order to participate in Single Family activities and to clarify what is allowed in calculating net development costs. The Denver Program Support Division will train all staff on the new requirements and how to review and interpret the year-end reports that are required and compare them to actual sales by utilizing SAMS reports.

Appendix B

Distribution

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The Honorable Joseph Lieberman, Ranking Member, Committee on Governmental Affairs, 706 Hart Senate Office Building, United States Senate, Washington, DC 20510

The Honorable Dan Burton, Chairman, Committee on Governmental Reform, 2185 Rayburn Bldg., House of Representatives, Washington, DC 20515

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Ms. Cindy Fogleman, Subcommittee on Oversight and Investigations, Room 212, O'Neil House Office Building, Washington, DC 20515

Director, Housing and Community Development Issue Area, United States General Accounting Office, 441 G Street, NW, Room 2474, Washington, DC 20548 (Attention: Stan Czerwinski)

Deputy Staff Director, Counsel, Subcommittee on Criminal Justice, Drug Policy and Urban Resources, B373 Rayburn House Office Building, Washington, DC 20515

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