



U.S. Department of Housing and Urban Development
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January 31, 2003

2003-FW-0801

MEMORANDUM FOR: Raynold Richardson
Director, Multifamily Housing Program Center, 6EHM

FROM: D. Michael Beard
Regional Inspector General for Audit, 6AGA

SUBJECT: HUD Houston Multifamily 's Oversight of Wood Hollow Place Apartments
Project Number 114-11183
Texas City, Texas

INTRODUCTION

We completed a limited review of HUD Houston Multifamily's oversight of Wood Hollow Place Apartments. The objective of the review was to determine whether Multifamily staff adequately monitored the project to ensure that the management agent complied with the Regulatory Agreement and HUD requirements.

METHODOLOGY AND SCOPE

While performing a review of Wood Hollow Place Apartments,¹ we noted potential monitoring deficiencies by the Houston HUD Multifamily office. As a result, we examined HUD's Multifamily project files for Wood Hollow Place Apartments from 1997 to 2002. We interviewed Multifamily staff to determine whether they pursued and corrected deficiencies. We also reviewed HUD Handbooks to obtain an understanding of Multifamily's monitoring responsibilities.

BACKGROUND

Wood Hollow Place Apartments, FHA Project 114-11183, is an 80-unit apartment complex located in Texas City, Texas. HUD originally insured the mortgage of Wood Hollow Place Apartments under Section 221(d)(4) of the National Housing Act. However, the owners refinanced the mortgage under Section 223(f) of the National Housing Act and signed a new

¹ OIG Report 2003-FW-1801, issued on November 18, 2002.

Regulatory Agreement with HUD on December 9, 1999. Since the refinancing, the project has experienced financial difficulties and been chronically delinquent in paying its mortgage.

Multifamily staff were aware that the project was chronically delinquent on its mortgage payments. Further, staff knew the owner had failed to submit required reports including audited financial statements and monthly accounting reports. As a result, Multifamily staff placed a flag on the owner's previous participation certificate. In addition, Multifamily staff recommended OIG review the project because they believed the owner might have improperly transferred money to other properties.

RESULTS OF REVIEW

The review disclosed two troubling conditions. Multifamily staff did not adequately monitor the project in three instances and did not properly maintain the project files. As a result, Multifamily personnel, including supervisors, did not discover or question payments that violated the Regulatory Agreement and HUD requirements.

Criteria. HUD Handbooks² provide guidance to Multifamily field office staff on how to oversee multifamily projects. The Handbooks specify that Multifamily staff must ensure that owners take actions to cure existing deficiencies, and that Multifamily staff continue monitoring while owners are correcting deficiencies. The Handbooks require Multifamily staff to follow up with the owner/management agent to obtain monthly reports. In addition, the Handbooks require Multifamily supervisors to establish a system for monitoring the receipt of the monthly accounting reports. The supervisors should also periodically check to see if staff receive and review the reports in a timely and quality manner.

Multifamily staff did not adequately monitor the project.

In three instances, Multifamily staff did not adequately monitor the project. In these cases, Multifamily staff did not perform sufficient work to ensure the owner complied with the Regulatory Agreement and HUD requirements. As a result, the owner made improper distributions totaling \$258,557 and failed to submit required reports.

Multifamily staff failed to follow up on improper distributions made in 1995 and 1996

In a 1997 letter, HUD Multifamily staff correctly questioned the management agent about distributions to the owner because the project did not have surplus cash. Less than 2 weeks later, the management agent responded that, "the funds were not a distribution, but the repayment of a bona-fide debt obligation." The former financial analyst failed to follow up on the management agent's response. In addition, Multifamily's project files lacked any records showing whether Multifamily agreed with the management agent's response or not. Our review subsequently disclosed the payments were improper distributions.

² HUD Handbook 4350.1 Rev-1, Multifamily Asset Management and Project Servicing, and HUD Handbook 4370.1 Rev-2, Reviewing Annual and Monthly Financial Reports.

HUD staff failed to ensure the management agent submitted required reports.

On two occasions, the former project manager failed to obtain required reports. He did not obtain 1998 audited financial statements and monthly accounting reports.

Audited Financial Statements. According to the former project manager's note in HUD's Real Estate Management System (REMS), HUD directed the owner to submit 1998 audited financial statements to HUD for review. The former project manager admitted he did not follow up on obtaining the financial statements. The new project manager obtained the 1998 financial statements in mid-2002 when HUD's Enforcement Center requested them.

Monthly Accounting Reports. Because the owner was in technical default of the mortgage, Multifamily required the owner to submit monthly accounting reports starting with May 31, 2001. On July 23, 2001, the owner agreed to provide monthly accounting reports to HUD. HUD received two monthly accounting reports. Then, the owner stopped submitting them. Although the former project manager stated he spoke with the management agent on several occasions, he did not document what, if any, actions he took to obtain the monthly accounting reports. By not following up and obtaining these reports, HUD could not review and correct improper disbursements being made by the management agent.

HUD did not properly maintain the project files.

Multifamily's former project manager could not locate the two monthly accounting reports he had received. In addition, he did not maintain a control log to track and monitor the receipt of the monthly accounting reports in REMS. The former project manager and his supervisor could not provide an adequate explanation for a lack of a log or the missing reports. Since the project manager did not properly maintain the files, he hampered HUD's ability to adequately monitor the project.

AUDITEE COMMENTS

The Director of the Houston Multifamily office provided us his written response on January 22, 2003. He agreed that the errors had occurred and stated that they should not have happened. In addition, he implemented the recommendations. He also elaborated that due to his office obtaining an additional supervisor, he believes the office is in a better position to perform its compliance, monitoring, and oversight functions more efficiently and effectively. The comments are attached.

RECOMMENDATIONS

We recommend that HUD's Houston Multifamily office:

1. Establish a monitoring system to ensure that Wood Hollow's project owners correct the deficiencies identified in our audit memorandum;
2. Establish controls over all project files to ensure they are properly maintained and safeguarded; and
3. Ensure that staff who did not perform their monitoring duties adequately receive direction, including training if necessary, on how to properly perform their duties. Further, if staff continue to perform inadequate monitoring, HUD should take appropriate actions against the employees.

Management comments are attached and include management decisions, planned actions and planned action dates. No further action is required.

Should you or your staff have any questions, please contact Theresa Carroll, Assistant Regional Inspector General for Audit, at (817) 978- 9309.

ATTACHMENT



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January 22, 2003

MEMORANDUM FOR: D. Michael Beard, Regional Inspector General for Audit, 6AGA

FROM:  Raymond Richardson, Director, Multifamily Housing Program Center, 6EHM

SUBJECT: HUD/FHA 114-11183 – HUD's Oversight of Wood Hollow Place Apartments
 Texas City, Texas

This is in response to your memorandum dated January 2, 2003, regarding the subject. Several of your recommendations have already been implemented due to the Asset Management Branch obtaining an additional Supervisor February 2002 to assist with the day-to-day operation. We are in a better position today to efficiently and effectively perform our compliance, monitoring and oversight function, as the supervisor ratio is 1:9 instead of 1:20 as in the past.

1 – Corrective Action Taken: This project was assigned to one of our more experienced Project Manager (PM), December 2002. Director instructed Asset Management Supervisors by memorandum January 7, 2003 (copy enclosed), to implement a system and control relative the OIG recommendations. Asset Management Supervisors provided response dated January 21, 2003 (copy enclosed). Our memorandum to you dated December 27, 2002, provided our management decisions to you regarding the timeframe the owner must adhere to relative all recommendations from your office. Final deadline for owner/agent with regard to all findings/recommendations is February 10, 2003.

Proposed Corrective Action and The Date To Be Completed: Effective date January 21, 2003, in accordance with memorandum from Director to Asset Management Supervisors.

Why Action is Considered Unnecessary: N/A

2 – Corrective Action Taken: Director instructed Asset Management Supervisors by memorandum January 7, 2003, to implement a system and control relative the OIG recommendations. Asset Management Supervisors provided response dated January 21, 2003. In addition, May 2002, management established a Workflow Committee, which devised a strategy for all project files, which has been implemented. These files have a definite protocol for document arrangement and storage, and all project files are in the process of converting to the new protocol, with a final date for completion January 2003. Management will review the new file system randomly throughout the year, especially those assets that are troubled and potentially troubled. Each year prior to Progress Reviews/Performance Ratings (EPPES) being communicated PM's, a formal review will take place with the PM and will be matched to REMS entries.

ATTACHMENT

For FY 2003, branch management has established three types of project teams: a Troubled Properties Team, consisting of the most experienced staff in physical and financial analysis; a Potentially Troubled Team, consisting of staff that are experienced but require additional technical training (this staff cross-train with the Troubled Properties Team); and a New Properties Team, which is staffed with experienced personnel who excel in customer service techniques, which is charged with ensuring all new owners and managing agents understand HUD requirements.

Proposed Corrective Action and The Date To Be Completed: Effective date January 21, 2003, in accordance with memorandum from Director to Asset Management Supervisors.

Why Action is Considered Unnecessary: N/A

3 – Corrective Action Taken: Director instructed Asset Management Supervisors by memorandum January 7, 2003, to implement a system and control relative the OIG recommendations. Asset Management Supervisors provided response dated January 21, 2003. A protocol for regular meetings was established in 2002. Quarterly Branch meetings and Management Review meetings are mandatory; weekly discussion meetings have been implemented for case discussions. In addition, team meetings are held at least monthly. Training-specific meetings are held, as courses/classes become available, including satellite broadcasts and on-site speakers/trainers. Financial Analysis Training was conducted in Headquarters September 24-26, 2002. The Houston Office attendee at this training conducted staff training for Houston October 30, 2002. Satellite training has been scheduled with regard to Basic Principals of Asset Management will be conducted March 2003 and Turning Around Troubled Assets will be conducted May 2003 by Headquarters. Houston PM staff will attend this training as designated. In 2002, Attorneys with the U.S. Department of Justice agreed to provide training with the Houston Office's General Counsel, for PM's on Building an Administrative Record. This training was scheduled for January 2003 but was postponed due to a family emergency for the USDJ attorney until February 2003.

The HUD Monitoring Desk Guide: Policies and Procedures for Program Oversight were published in conjunction with the FY 2000 Compliance and Monitoring Training. This document will be reviewed during our mid-year and end of the year Risk Assessments. If staff should continue to perform inadequate monitoring, this office will take the appropriate actions as delineated by outstanding HUD handbooks and guidelines.

Proposed Corrective Action and The Date To Be Completed: Effective date January 21, 2003, in accordance with memorandum from Director to Asset Management Supervisors.

Why Action is Considered Unnecessary: N/A

If you have additional concerns, please contact me at (713) 313-2274 extension 7063.

Enclosures

cc: McGuigan 6EHMA
Carter 6EHMA

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