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Audit-Related Memorandum
98-SE-107-0807

April 16, 1998

To: Jacqueline Johnson, Deputy Assistant Secretary for Office of Native American Programs, PI

From: A. George Tilley, District Inspector General for Audit, OAGA

Subject: Northwest Office of Native American Programs
Oversight of Southern Puget Sound Inter-Tribal Housing Authority
Seattle, Washington

On November 29, 1996, OIG received a request from the Secretary of HUD to thoroughly review allegations of various improprieties in the use of HUD funds by Tribal governments and/or Indian housing authorities (IHAs) and inadequate monitoring by HUD's Office of Native American Programs (ONAP). Program abuse at IHAs across the country was alleged in *The Seattle Times'* December 1996 series of articles entitled "From deregulation to disgrace" which identified 29 instances. The series included allegations that a \$1.2 million housing grant to the Southern Puget Sound Inter-Tribal Housing Authority bought a polluted, unusable piece of property and built a large home for the tribal chairman.

Audit Objective, Scope and Methodology

As part of our review to address the Secretary's request, we wanted to know if the Northwest Office of Native American Programs (NWONAP) provided effective oversight of the Southern Puget Sound Inter-Tribal Housing Authority (IHA). To accomplish this, we:

- reviewed *The Seattle Times* series.
- contacted the NWONAP Administrator to obtain:

- * a perspective and position on the issues reported in *The Seattle Times* series for the IHA,
 - * a description of the program requirements applicable to the IHA, and
 - * a description of actions taken by NWONAP in relation to the issues reported in the series for this IHA.
- obtained and reviewed applicable program requirements including statutes, regulations, handbooks, guidebooks, memoranda, and other directives.
 - interviewed appropriate staff, and reviewed available documentation related to oversight. The review included testing of the management information and control systems to obtain an understanding of how those systems functioned.
 - compared the oversight and actions taken by the NWONAP to the applicable requirements.

We performed our field work from February through April 1997, and extended our work as necessary to accomplish our objective. This work was a part of the work done to address the Secretarial request discussed above. This memorandum includes specific recommendations that were not within the scope of the audit report responding to the Secretarial request (Report 98-SE-107-0002).

Audit Results

Our review disclosed that NWONAP oversight of the IHA did not ensure development requirements were met. A required environmental review was not obtained prior to releasing funds for purchase of a commitment to provide a leasehold and Low-rent funds were permitted to be used as Mutual Help funds. As a result:

- The IHA spent \$205,000 for a commitment to enter into a leasehold on a polluted site that cannot be used to develop the planned ten units of Low-rent housing until another \$468,000 is spent to remove the contaminants. Also, the IHA spent an additional \$31,235 to identify and remove a portion of the hazardous pollutants from this land even though a leasehold had not been obtained.
- The IHA sold houses developed with Low-rent development funds to Tribal members for \$531,729¹ less than the \$749,295 it cost to develop

¹ \$391,000 of the \$531,729 is secured by forgivable second mortgages. These second mortgages are forgiven over a ten year period.

them. Accordingly, the ten intended Low-rent units were not developed. Also, the Tribal Chairman, who was not low income and not eligible for the Low-rent program, benefited from the IHA's action, receiving a 2,100 square foot, \$176,405 custom two story home that he lived in without making any payments for the first 11 months.

Required Environmental Review Not Obtained

Federal regulations at 24 CFR 50, and HUD Handbook 7450.1 state that HUD is responsible for completing an environmental assessment prior to expending other than planning funds on a project. These requirements are reiterated in HUD Development Handbook 7450.1, REV-1.

NWONAP did not complete an environmental review before permitting the IHA to advance the Tribe \$205,000.

On December 22, 1993, the IHA requested \$205,000 of its \$1.2 million Low-rent development grant to purchase a leasehold on a proposed housing site for 10 of the 30 units included in the grant. The approved development plan allocated these ten units to the Shoalwater Bay Indian Tribe. On December 27, 1993, NWONAP approved the \$205,000 disbursement to the IHA subject to five conditions, one being that HUD would complete its environmental review. The IHA did not meet these five conditions before paying the \$205,000 to the Shoalwater Bay Indian Tribe for the leasehold. Also, the NWONAP did not question the IHA's use of the funds even though HUD had not completed the required environmental review.

The polluted site cannot be used to develop the needed ten units of Low-rent housing until contaminants are removed.

In 1997, the Environmental Protection Agency determined that the site cannot be used for housing until contaminants are removed at a cost of about \$468,000. Prior to the Environmental Protection Agency review the IHA had obtained a level two environmental review at a cost of \$25,373 which identified chemical and petroleum hazards, and paid \$5,862 to a contractor for removal of some of the contaminants. Also, the property cannot be placed in trust because of the pollution. Accordingly, the Tribe could not provide the IHA a leasehold and had not provided a written commitment to provide a leasehold. (We noted that the IHA advanced the funds to the Tribe in exchange for a commitment to provide a leasehold. As of July 1997, the IHA has not yet received a leasehold on the land.)

NWONAP's Director of Development, who was aware of the requirements, placed a higher priority on starting the Low-rent development project than on ensuring the site was environmentally safe.

The Director of Development (at the time) stated that he approved the disbursement although he knew that an environmental review should have been done. He stated he approved the disbursement without doing the required review for several reasons. First, the IHA had been trying for three years to obtain an approved site and had unsuccessfully attempted to purchase three sites. Second, NWONAP assumed the land could be (and needed to be) quickly purchased and placed into trust and that all parties were unaware of any items which would impede the process.

Low-rent funds were permitted to be used as Mutual Help funds

The regulations at 24 CFR 950.455 state that an IHA may apply to the HUD Area ONAP for approval to convert any or all of the units in an existing rental project to the Mutual Help program. The application process requires the IHA to submit a request for conversion to the HUD Area ONAP. The HUD Area ONAP must review the application for legal sufficiency; tribal acceptance; demonstration of family interest; evidence that units are habitable, safe, and sanitary; family qualifications; and financial feasibility. HUD also has provisions for converting a rental project to the Mutual Help program prior to development of the project. This is referred to as reformulation and requires HUD approval. The preamble to the Federal Register publication of the final rule part 950 addressed reformulation as follows:

- Consistent with other grant programs, if an IHA wishes to redirect project funds, a program modification must be proposed and approved before such reformulation can proceed.

NWONAP allowed the IHA to use Low-rent development funds as if they were Mutual Help homeownership development funds.

The NWONAP denied an IHA request to reformulate the Low-rent development to a Mutual Help development. Instead of officially reformulating the development NWONAP simply allowed the IHA to sell houses developed with Low-rent development funds to participants as if they were Mutual Help development funds. These houses were developed with funds allocated by the development plan to the Shoalwater Bay Indian Tribe. The IHA had planned to convert the houses from Low-rent to Mutual Help and the NWONAP Administrator understood that if an IHA is planning to convert a rental project to Mutual Help, it should treat it as Mutual Help from the start. The IHA's Executive Director's notes from a January 1996 meeting with HUD show the NWONAP Administrator suggested the IHA execute Mutual Help leases for the units it was acquiring.

As a result, the IHA sold seven Tribal members houses for \$531,729² less than the \$749,295 it cost to develop them and the ten intended Low-rent units were not developed.

Seven Tribal members purchased houses developed with Low-rent funds for at least \$531,729³ less than the \$749,295 it cost to develop them. Since these seven homes were built with Low-rent development funds and were not converted to the Mutual Help program, the disposition should have followed the rules in 24 CFR 950 Subpart M for disposal of Low-rent dwelling units. Those rules and the Annual Contribution Contract require HUD approval of the disposition and sale at fair market value.

The Tribal Chairman, who was not low income, received the greatest benefit.

The IHA's records show the Tribal Chairman had an income of at least \$13,000 over the low income limits when he applied for Low-rent housing in 1994. The Chairman received the largest house under the program, at 2,100 square feet and at a cost to the IHA of \$176,405. The IHA sold the home to the Chairman for \$76,184. The IHA has had the \$76,184 first mortgage for sale since the Chairman moved in during April 1996. Additionally, the IHA did not require the Chairman to make any mortgage or rental payments for the first 11 months he lived in the home.

This occurred because NWONAP's Administrator placed a higher priority on the flexibility in the regulations than on following the rules of the program.

The NWONAP Administrator allowed the IHA's program to go forward in the spirit of increased flexibility. He stated that he depended on the IHA's prior Executive Director's assurances that the program complied with regulations. Also, the NWONAP Administrator relied on the verbal assurances of a staff member and instructions he thought were from Headquarters that Low-rent projects could be treated as Mutual Help projects right from the start if an IHA intended to convert. However, the Low-rent requirements state that the reformulation (during development) must go through a re-rating and re-ranking process before being approved by ONAP. ONAP Headquarters staff confirmed that unless the IHA applies and the Field Office approves a change, a Low-rent project may not be treated as Mutual Help. The Deputy Assistant Secretary for Native American Programs stated that to be fair, they do not want IHAs to be able to change the type of development at will, therefore they need to go through reformulation.

² \$391,000 of the \$531,729 is secured by forgivable second mortgages. These second mortgages are forgiven over a ten year period.

³ i.b.i.d.

The NWONAP's actions allowed ineligible expenditures totaling \$236,235 for a polluted site and the sale of houses built with Low-rent funds for \$531,729⁴ less than the \$749,295 they cost. These actions have reduced the number of housing units provided to eligible participants. We believe that these conditions should be corrected consistent with the requirements of the US Housing Act of 1937. However, we recognize that the Native American Housing and Self Determination Act of 1996 now governs HUD's Native American Housing programs and will govern the use of any funds repaid to the program.

AUDITEE COMMENTS AND OIG EVALUATION

NWONAP agreed with the facts as they are presented. However, NWONAP strongly disagreed with the conclusions drawn. NWONAP's written comments are included in the Attachment.

Auditee Comments

NWONAP disagrees that it should require the IHA to reimburse its Low-rent program for the \$749,297 in misused funds that were intended to develop ten needed units of Low-rent housing. NWONAP let the IHA treat the Low-rent housing project as a Mutual Help homeownership program. NWONAP insists that the IHA achieved the Low-rent program objectives when Native Americans were housed.

OIG Evaluation

We do not agree with NWONAP that the IHAs program provided the housing needed by the low income Native American population it was intended to assist. Rather, three of the seven houses went to over income Native Americans at the expense of low income Native Americans.

The Low-rent and Mutual Help programs are intended to serve different segments of the low income Native American population. Therefore, a change from one program to the other changes the intended beneficiaries. The differences in intended beneficiaries are clearly shown by the eligibility requirements of the programs. The eligibility requirements of the programs are that:

- The Low-rent program must meet the housing needs of low income families. In this case the IHA received a Low-rent program grant to address the housing needs identified in the IHAs application. This grant

⁴ \$391,000 of the \$531,729 is secured by forgivable second mortgages. These second mortgages are forgiven over a ten year period.

provided funding to develop assisted “rental housing” that would be affordable to low income families for the life of the project. The low income families payments for affordable housing would have equaled 30 percent of their adjusted income, and including rent and utilities.

- The Mutual Help homeownership program was designed to meet the homeownership needs of low income families that have difficulty accessing the private mortgage market. The program also allows a limited number of over income families, if the Indian Housing Authority demonstrates a need and qualifies for an exception. The exception allows the participation of over income families if the housing authority demonstrates to HUD’s satisfaction that there is a need to house over income families that cannot reasonably be met without such assistance. In addition, the number of over income exceptions is limited by statute to the greater of ten percent of the units in the project or five units.

Families in the Mutual Help program must be willing and able to meet the obligations that homeownership includes. The family must be willing and able to perform or provide needed home maintenance, provide the required Mutual Help Contribution (\$1,500), and pay for utilities and the administration charge. Not all low income families are willing or able to meet these obligations. In the IHA’s program two low income families lost their houses because they were not willing or able to meet these obligations.

The IHA’s innovative program was intended to leverage the funding and allow homeownership assistance to more than ten low income families. As implemented, the program produced only seven houses for seven families. Only two low income Native American families are being assisted by the program. For the remaining five families, three are not low income and two have lost their houses.

Recommendations

We recommend that NWONAP:

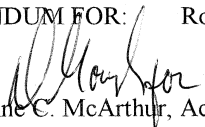
- A. obtain a legal opinion on the propriety of requiring the IHA to reimburse its housing program the \$236,235 and any additional costs associated with purchase and environmental clean up of the polluted site.
- B. ensure required environmental reviews are completed prior to the expenditure of HUD funds.
- C. obtain a legal opinion on the propriety of requiring the IHA to reimburse its housing program \$749,297 for the development costs of the seven Low-rent units that were sold.
- D. If it is determined inappropriate to have the IHA reimburse its program for the seven units, require the IHA to determine the eligibility of all seven participants, and reimburse the program for assistance to any ineligible participants.
- E. ensure that future decisions are based on facts and documented guidance, if necessary, rather than what is believed to be allowable.
- F. evaluate the inappropriate approval of the project site and take actions deemed appropriate to hold persons accountable for their actions.
- G. evaluate the inappropriate approval allowing the IHA to treat the Low-rent project as Mutual Help and take actions deemed appropriate to hold persons accountable for their actions.



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March 26, 1998

MEMORANDUM FOR: Robert H. Woodard, Assistant District Inspector General for Audit

FROM:  Jeanne C. McArthur, Acting Administrator, Northwest Office of Native American Programs, OAPIB

Subject: Comments on Oversight of Southern Puget Sound Inter-Tribal Housing Authority

The Office of Native American Programs has reviewed the above referenced document and offer the following comments:

Where we agree with the facts as they are presented, we strongly disagree with the conclusions drawn. We do not agree that the SPSITHA somehow deprived low income families of needed housing by converting a Low Income Rental project To Mutual Help and that they (SPSITHA) should reimburse \$749,297.00. This is an activity that was allowable at the time of the transactions. They may not have followed procedures properly but satisfied the intent. This office was aware of the conversion and, in fact, participated in it. We agree that a legal opinion will clarify the recommendation.

On your recommendation 1.A., having to do with environmental clean up; resolution will depend largely on the ultimate disposition of the property. A management decision will be reached when final decisions are made.

We agree with 1.C. and 1.D.

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