



Yorkville Cooperative, Fairfax, VA

HUD-Insured Multifamily Rental Housing for Moderate-Income Families



To: Brenda Brown, Director, Asset Management Division, Baltimore Multifamily Hub, 3BHMLAP

Craig T. Clemmensen, Director, Departmental Enforcement Center, CV
//signed//

From: David E. Kasperowicz, Regional Inspector General for Audit, Philadelphia Region, 3AGA

Subject: The Yorkville Cooperative, Fairfax, VA, Did Not Administer Its HUD-Insured Property and Housing Assistance Contract According to Applicable Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the Yorkville Cooperative's administration of its HUD-insured property and housing assistance contract.

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

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

If you have any questions or comments about this report, please do not hesitate to call me at 215-430-6734.



Audit Report Number: 2017-PH-1003

Date: May 22, 2017

The Yorkville Cooperative, Fairfax, VA, Did Not Administer Its HUD-Insured Property and Housing Assistance Contract According to Applicable Requirements

Highlights

What We Audited and Why

We audited the Yorkville Cooperative's administration of its U.S. Department of Housing and Urban Development (HUD)-insured property and housing assistance contract based on a complaint alleging that the Cooperative (1) spent excessive amounts for maintenance and repairs and (2) did not recertify tenants in a timely manner. Our objective was to determine whether the Cooperative administered its HUD-insured property and housing assistance contract according to applicable requirements.

What We Found

The Cooperative did not always administer its HUD-insured property and housing assistance contract in accordance with its regulatory agreement and applicable HUD requirements. Specifically, it (1) did not always obtain the required number of written cost estimates or have documentation to support payments for products and services, including maintenance and repair work on units totaling more than \$1.8 million, and (2) it paid nearly \$297,000 for prohibited legal services. It also did not ensure that it correctly calculated housing assistance payments. The payments for prohibited legal services and the inaccurate housing assistance payments are repeat findings from our 2009 audit of the Cooperative.¹

What We Recommend

We recommend that HUD direct the Cooperative to (1) provide documentation to support payments totaling more than \$1.8 million or reimburse the project from nonproject funds for amounts that it cannot support and (2) reimburse the project nearly \$297,000 from nonproject funds for the ineligible legal expenses. Also, from our previous audit report, we will reopen recommendations that HUD direct the Cooperative to develop and implement procedures to ensure that (1) disbursements made from its operating account are for expenses that are reasonable, necessary, and in accordance with program requirements and (2) housing assistance payments are correctly calculated and supported with the required documentation.

¹ Audit Report 2010-PH-1003, The Yorkville Cooperative, Fairfax, VA, Did Not Administer Its Section 221(d)(3) Property and Housing Assistance Contract According to Its Regulatory Agreement and HUD Requirements, issued November 25, 2009

Table of Contents

Background and Objective.....	3
Results of Audit	4
Finding 1: The Cooperative’s Payments for Products and Services Did Not Always Comply With Requirements	4
Finding 2: The Cooperative Did Not Implement Recommended Corrective Actions From Our Prior Audit Report	7
Scope and Methodology.....	10
Internal Controls.....	12
Appendixes.....	14
A. Schedule of Questioned Costs	14
B. Auditee Comments and OIG’s Evaluation.....	15
C. Results of Payment Review	27

Background and Objective

The Yorkville Cooperative was organized on July 15, 1977, for the purpose of acquiring, rehabilitating, and operating as a cooperative housing project under Section 221(d)(3) of the National Housing Act. The affairs of the Cooperative are governed by a board of directors, which consists of five members. The Cooperative is located at 3146 Draper Drive, Fairfax, VA.

The U.S. Department of Housing and Urban Development (HUD) entered into a regulatory agreement with the Cooperative in 1979 for mortgage insurance under HUD's Section 221(d)(3) program. The program insures mortgage loans to finance multifamily rental housing for moderate-income households, including projects designated for the elderly. The regulatory agreement provided the Cooperative housing assistance contracts for its units. The Cooperative executed a Section 8 contract with HUD for 236 units. Currently, 228 of the 236 units are occupied, and 8 are vacant. During our audit period, HUD provided the Cooperative the following housing assistance funds:

Fiscal year	Housing assistance funds provided
2015	\$2,345,510
2016	2,595,637
Total	4,941,147

In June 2016, we received a complaint alleging that the Cooperative (1) spent excessive amounts for maintenance and repairs, (2) had accounts receivable balance of more than \$300,000, including \$4,500 owed by its board president despite not residing on the property, (3) was not recertifying tenants timely, and (4) allowed the physical condition of the property to deteriorate. HUD was addressing the allegation regarding the accounts receivable. We could not substantiate the allegation regarding the physical condition of the property. We found the property to be in good physical condition.

Our objective was to determine whether the Cooperative administered its HUD-insured property and housing assistance contract according to applicable requirements.

Results of Audit

Finding 1: The Cooperative's Payments for Products and Services Did Not Always Comply With Requirements

The Cooperative did not always (1) obtain the required number of written cost estimates before making purchases; (2) ensure that vendors performing maintenance and repairs on units were properly licensed as required; and (3) have documentation to support payments for products and services, including maintenance and repair work on units. These conditions occurred because the Cooperative lacked written procedures to ensure that it complied with its regulatory agreement and applicable requirements. As a result, it could not show that more than \$1.8 million paid for products and services was for costs that were fair and reasonable and for work that was performed and that the work performed complied with applicable building codes.

The Cooperative Did Not Always Obtain the Required Number of Written Cost Estimates

The Cooperative did not always ensure that it obtained the required number of written cost estimates before paying nearly \$1.8 million to six vendors for such things as unit repairs, maintenance supplies, and the replacement of heating and air conditioning units.² Paragraph 6.50(a) of HUD Handbook 4381.5, REV-2, requires the Cooperative to obtain written cost estimates from at least three contractors for any contract, supply, or service that is expected to exceed \$10,000 per year. The Handbook also requires the Cooperative to retain documentation of all bids for 3 years following the completion of the work. The regulatory agreement required the Cooperative to disburse funds from the operating account for only reasonable operating expenses and necessary repairs. This condition occurred because the Cooperative did not have written procedures to ensure that it obtained written cost estimates. As a result, it could not show that the nearly \$1.8 million paid to six vendors for products and services was for fair and reasonable costs.

Vendors Were Not Always Properly Licensed

The Cooperative did not ensure that two vendors paid \$725,738 were properly licensed.³ The vendors performed maintenance and repair work on units. However, they were not licensed as required. Chapter 11 of Title 54.1 of the Virginia Code requires a license for any person performing or managing construction, removal, repair, or improvement work when the value of the contract exceeds \$1,000. This condition occurred because the Cooperative did not have written procedures to ensure that vendors were properly licensed. Without proper licensing, the Cooperative had no assurance that the work performed complied with applicable building codes.

² See appendix C for details.

³ Ibid.

Payments to Vendors Were Not Always Supported

The Cooperative did not have support for \$163,885 paid to three vendors.⁴ Its vendor payment files did not contain invoices to support the payments. Section 12(c) of the Cooperative's regulatory agreement required it to maintain documentation in a reasonable condition for audit or inspection. This condition occurred because the Cooperative did not have written procedures to ensure to that it obtained supporting documentation before paying for products and services. Without the invoices, the \$163,885 in payments was unsupported.

Conclusion

The Cooperative did not always (1) obtain the required number of written cost estimates before making purchases; (2) ensure that vendors performing maintenance and repairs on units were properly licensed as required; and (3) have documentation to support payments for products and services, including maintenance and repair work on units. The conditions existed because the Cooperative lacked written procedures to ensure compliance with program requirements. As a result, the Cooperative could not show that more than \$1.8 million paid for products and services was for costs that were fair and reasonable and for work that was performed and that the work performed complied with applicable building codes.

Recommendations

We recommend that the Director, Asset Management Division, Baltimore Office of Multifamily Housing Programs, direct the Cooperative to

- 1A. Provide documentation to show that prices paid for purchases of products and services totaling \$970,381⁵ were fair and reasonable or reimburse the project from nonproject funds for any amounts that were not fair and reasonable.
- 1B. Provide documentation to show that payments for work totaling \$716,693⁶ complied with applicable building codes or reimburse the project from nonproject funds for payments that did not comply with the codes and take action to bring the work up to code.
- 1C. Provide documentation to support payments totaling \$163,885 or reimburse the project from nonproject funds for payments that it cannot support.
- 1D. Develop and implement written procedures to ensure that it obtains written cost estimates as required and maintains complete documentation to support

⁴ Ibid.

⁵ To avoid double-counting, we reduced the amount shown as unsupported for recommendation 1A by the amounts in recommendations 1B and 1C that also lacked cost estimates. The \$970,381 is the full amount related to purchases not supported by cost estimates (\$1,770,984) less \$636,718 reported in recommendation 1B and \$163,885 reported in recommendation 1C.

⁶ To avoid double-counting, we reduced the amount shown as unsupported for recommendation 1B by the amount in recommendation 1C for work that was performed by an unlicensed contractor. The \$716,693 is the full amount related to work performed by unlicensed contractors (\$725,738) less \$9,045 reported in recommendation 1C.

expenditures and that contractors performing or managing construction, removal, repair, or improvement work are properly licensed as required.

Finding 2: The Cooperative Did Not Implement Recommended Corrective Actions From Our Prior Audit Report

The Cooperative did not implement corrective actions for two recommendations from a prior audit report.⁷ It did not develop and implement adequate procedures and controls to ensure that disbursements made from its operating account were for expenses that were reasonable, necessary, and in accordance with program requirements. It also did not develop and implement procedures to ensure that housing assistance payments were correctly calculated and supported with the required documentation. This condition occurred because the Cooperative's board of directors did not provide proper oversight of the management agent to ensure that it implemented the agreed-upon corrective action to address recommendations from the prior audit. As a result, the Cooperative made ineligible payments totaling \$296,787 for prohibited legal services and \$3,892 in housing assistance overpayments.

The Cooperative Paid for Legal Services That Were Not Operating Expenses

In our prior audit report, we found that the Cooperative paid for ineligible legal expenses. Recommendation 1B required the Cooperative to develop and implement adequate procedures and controls to ensure that disbursements made from its operating account were only for reasonable, necessary costs and in accordance with program requirements. During the process to resolve the recommendations from the prior audit report, the Cooperative agreed that it would stop paying for legal services that were not operating expenses. However, the management agent did not implement procedures as agreed upon, and the Cooperative's board of directors did not provide proper oversight. Therefore, the Cooperative continued to pay for ineligible legal services. Specifically, it used funds from the operating account for legal services beyond those related to eviction procedures. During the period January 2012 to June 2016, the Cooperative paid a law firm \$296,787 from its operating account for legal services associated with representation at board and community meetings and for the review of business-related documents, such as proposals, contracts, membership handbooks, and documents associated with refinancing the property. None of the payments were related to eviction procedures. HUD Handbook 4370.2, REV-1, CHG-1, states that the legal expense account should be used to record legal fees for services incurred on behalf of the project, for example, legal fees for eviction procedures. HUD clarified this guidance to the Cooperative in May 2009, by informing it that the only legal fees it should be incurring and paying from operational income are fees incurred during an eviction process. Additionally, appendix 3b of HUD Handbook 4381.5, REV-2, states that the management agent will comply with HUD handbooks, notices, or other policy directives that relate to management of the project and ensure that all expenses of the project are reasonable and necessary. The legal services provided by the law firm were entity related, but they were not operating or reasonable expenses of the project.

⁷ Audit Report 2010-PH-1003, The Yorkville Cooperative, Fairfax, VA, Did Not Administer Its Section 221(d)(3) Property and Housing Assistance Contract According to Its Regulatory Agreement and HUD Requirements, issued November 25, 2009

The Cooperative Did Not Ensure That Housing Assistance Payments Were Always Calculated Correctly

In our prior audit report, we found that the Cooperative did not maintain adequate documentation to support housing assistance payments and made housing assistance overpayments.

Recommendation 2F required the Cooperative to develop and implement procedures to ensure that housing assistance payments were correctly calculated. These procedures, at a minimum, required the Cooperative to include a statement from management certifying that the housing assistance payment amounts were reviewed by management and prepared in accordance with HUD requirements. However, the management agent did not implement procedures as agreed upon, and the Cooperative's board of directors did not provide proper oversight. Therefore, the Cooperative did not perform supervisory reviews of initial, interim, and annual recertifications, and it continued to overpay housing assistance. The Cooperative incorrectly calculated income in 8 of 11 tenant files, resulting in overpayment of housing assistance totaling \$3,892 from January 2015 to December 2016.

HUD Handbook 4350.3, REV-1, CHG-4, HUD Handbook 4381.5, REV-2, and the regulatory agreement required the Cooperative and its management agent to ensure that the computation of tenant rents, assistance payments, recertifications, and other subsidy contract functions were performed in accordance with applicable requirements. Without adequate controls to ensure that housing assistance payments were correctly calculated, there was an increased risk that the Cooperative would continue to overpay.

Conclusion

The Cooperative did not implement two recommendations from a prior audit report. It paid for legal services that were not operating expenses of the project and did not develop and implement procedures to ensure that housing assistance payments were correctly calculated and supported with required documentation. This condition occurred because the Cooperative's board of directors did not provide proper oversight of the management agent to ensure that it implemented the agreed-upon corrective action to address recommendations from the prior audit. Because the Cooperative did not implement agreed-upon corrective actions, it made ineligible payments totaling \$296,787 for prohibited legal services and \$3,892 in housing assistance overpayments.

Recommendations

Based on the results of our review, we will reopen the following recommendations from audit report 2010-PH-1003:

Recommendation 1B. Develop and implement adequate procedures and controls to ensure that disbursements made from its operating account are for expenses that are reasonable, necessary, and in accordance with program requirements.

Recommendation 2F. Develop and implement procedures to ensure that housing assistance payments are correctly calculated and supported with the required documentation. The procedures, at a minimum, should include a statement from management certifying that the determined housing assistance payment amounts have been reviewed by management and were prepared in accordance with HUD requirements.

In addition, in this report, we recommend that the Director, Asset Management Division, Baltimore Office of Multifamily Housing Programs, direct the Cooperative to

- 2A. Reimburse the project \$296,787 from nonproject funds for the ineligible legal expenses.
- 2B. Reimburse HUD \$3,892 from nonproject funds for the overpayment of housing assistance.
- 2C. Correct the errors in the tenant files identified during the audit.

We also recommend that the Director of HUD's Departmental Enforcement Center

- 2D. Review the issues identified in this audit report and if appropriate, pursue administrative sanctions against the board of directors for the violations cited in this report.

Scope and Methodology

We conducted the audit from July 2016 through March 2017 at the Yorkville Cooperative located in Fairfax, VA, and our offices located in Richmond, VA, and Baltimore, MD. The audit covered the period January 1, 2015, through June 30, 2016, but was expanded when necessary. To accomplish our objective, we reviewed

- The Cooperative's regulatory agreement.
- HUD Handbooks 4350.1, REV-1; 4350.3, REV-1, CHG-4; 4370.2, REV-1, CH-1; and 4381.5, REV-2.
- Form HUD-9839-B, Project Owner's and Management Agent's Certification for Multifamily Housing Projects for Identity-of-Interest or Independent Management Agents.
- The Cooperative's accounting records; audited financial statements for 2015 and 2016; vendor files; invoices; tenant files; computerized databases, including the housing assistance payment register and the general ledger; board meeting minutes from January 1, 2015, to June 30, 2016; organization charts; and housing assistance payments contract.
- HUD's monitoring reports for the Cooperative.
- Tenant files for the five members of the Cooperative's board to determine whether they were eligible for housing assistance and the assistance amount was calculated accurately.
- Tenant files for six families with the latest move-in dates to determine whether they were eligible for housing assistance and the assistance amount was calculated accurately.
- Vendor licensing information from the State of Virginia Department of Labor's website.

We also interviewed the Cooperative's employees and HUD staff.

We analyzed the Cooperative's check register and identified the vendors to whom the Cooperative paid more than \$100,000 during our audit period. We selected the 10 vendors with the largest amounts of payments to determine whether the Cooperative disbursed funds only for operating expenses that were reasonable and necessary in accordance with applicable requirements. These 10 vendors received nearly \$3.7 million during our audit period (appendix C).

We reviewed 11 tenant files to determine whether the families were eligible for assistance and the housing assistance payments were accurately calculated and supported. Using the Tenant Rental Assistance Certification System, we identified the 10 families with the latest move-in dates, and from that list, we selected every other family plus 1 for a total of 6 families to review. We also selected the files for the five members of the Cooperative's board.

To achieve our objective, we relied in part on computer-processed data. We used information on the Cooperative's general ledger to identify vendors to whom it paid more than \$100,000 and payments for legal services during the audit period. We also used the Authority's check register

to identify payments to vendors, and we reviewed tenant ledgers to identify housing assistance payments, admission dates, and rent amounts. Although we did not perform a detailed assessment of the reliability of the data, we did perform a minimal level of testing and found the data to be adequate for our purposes.

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

Internal Controls

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

- effectiveness and efficiency of operations,
- reliability of financial reporting, and
- compliance with applicable laws and regulations.

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

Relevant Internal Controls

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

- Effectiveness and efficiency of operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Reliability of financial information – Policies and procedures that management has implemented to reasonably ensure that it obtains relevant and reliable information to adequately support program expenditures and discloses that information in the required reports.
- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that program expenses are supported and comply with program funding guidelines and restrictions.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The Cooperative lacked written procedures to ensure compliance with applicable HUD requirements and its regulatory agreement. (finding 1)

- The Cooperative's board of directors did not provide proper oversight of the management agent to ensure that it implemented the agreed-upon corrective action to address recommendations from a prior audit. (finding 2)

Appendixes

Appendix A

Schedule of Questioned Costs

Recommendation number	Ineligible 1/	Unsupported 2/
1A		\$970,381 ⁸
1B		716,693 ⁹
1C		163,885
2A	\$296,787	
2B	3,892	
Totals	300,679	1,850,959

- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.
- 2/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

⁸ To avoid double-counting, we reduced the amount shown as unsupported for recommendation 1A by the amounts in recommendations 1B and 1C that also lacked cost estimates. The \$970,381 is the full amount related to purchases not supported by cost estimates (\$1,770,984) less \$636,718 reported in recommendation 1B and \$163,885 reported in recommendation 1C.

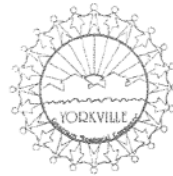
⁹ To avoid double-counting, we reduced the amount shown as unsupported for recommendation 1B by the amount in recommendation 1C for work that was performed by an unlicensed contractor. The \$716,693 is the full amount related to work performed by unlicensed contractors (\$725,738) less \$9,045 reported in recommendation 1C.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments



YORKVILLE
Board of Directors
3146 Draper Drive
Fairfax, VA 22031
(703) 273-7777

May 3, 2017

VIA ELECTRONIC & FIRST-CLASS MAIL

Mr. David E. Kasperowicz
Regional Inspector General for Audit
HUD-OIG Office of Audit, Philadelphia Region
100 Penn Square East, Suite 10205
Philadelphia, PA 19107

Re: Yorkville Cooperative, Fairfax VA
Auditee Comments to Draft Audit Report

Dear Mr. Kasperowicz:

This letter is our response to the draft Audit Report sent on April 11, 2017 for the Yorkville Cooperative ("Yorkville") located at 3146 Draper Drive, Fairfax, Virginia 22031. We understand that this letter will be published along with the final report; we trust you will consider the contents of this response and amend the final Audit Report accordingly. As previously discussed with you, we disagree with the finding of the draft Audit Report that Yorkville paid for legal services that were not operating expenses. Additionally, although Yorkville's Board of Directors (the "Board") acknowledges its ultimate responsibility in ensuring that Yorkville administers its HUD-insured property and housing assistance contract according to applicable requirements, we believe the report did not adequately address the actions the Board took towards ensuring Yorkville was administered properly.

In order to understand our position on your Findings and Recommendations, it is important to provide some context. It is our belief that your office did not provide sufficient weight to our unique circumstances.

Yorkville Cooperative is a residential cooperative housing community designed to serve low income families and individuals. It is governed and operated by a Board of five (5) Directors elected by Yorkville's residents. These Directors, all residents of the community, are volunteers and are not paid for the countless hours they spend working for the community. The Directors come from various cultural and educational backgrounds and sometimes have difficulty

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Mr. David E. Kasperowicz
May 3, 2017
Page 2 of 6

communicating in English. Yorkville did not choose this system of operation, but it has persevered for almost forty (40) years and remains a strong and successful community.

Due to the nature of Yorkville's residents, its organizational structure, and HUD requirements, the Board of Directors has continuously contracted with highly respected professional management companies who are experienced and conversant with many requirements established by the Department of Housing and Urban Development ("HUD"). Additionally, the Board has worked with experienced legal counsel to further advise and assist them regarding matters pertaining to the operation of the project. Yorkville's attorneys and management agents have been invaluable to the Board's efforts to provide good housing, support a safe and viable community, and meet all legal requirements as they arise. In fact, particularly due to the wide-ranging characteristics of the Board, we believe it would be a breach of our fiduciary duty to Yorkville if the Board made decisions regarding the property without consulting with professionals first. The issue this creates, however, is that the Board's reliance on its professionals, particularly its management agent who conducts the day-to-day operations of the property, depends on the professionals' ability to administer their tasks properly.

With this in mind, the following are our responses to each finding:

Finding 1: The Cooperative's Payments for Products and Services Did Not Always Comply With Requirements

Response:

Finding 1 of the draft Audit Report attributed three (3) sub-findings to Yorkville. The first such sub-finding was that Yorkville "did not always obtain the required number of written cost estimates." As explained above, Yorkville contracts with a professional management agent to provide the day-to-day operations of the property. During the stated audit period (January 1, 2015 through June 30, 2016), Yorkville contracted with a professional management agent. In the management contracts for Yorkville, the management agent was obligated to, among other things, comply with all HUD requirements. One specific responsibility assigned to the management agent was to obtain at least three (3) written cost estimates from various contractors for any contract, supply, or service expected to exceed \$10,000, in compliance with Paragraph 6.50(a) of HUD Handbook 4381.5.

The audit determined that the required number of written cost estimates was not always obtained. Yorkville's Board of Directors acknowledges their ultimate responsibility for Yorkville's compliance with the applicable requirements. However, it is important to recognize that the obligation for such compliance was delegated to a management agent that was approved by HUD. Additionally, Yorkville's Board of Directors proactively contacted its management agent in mid-June 2016 requesting clarification on their procedures and process for capital

Comment 1

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 1

Mr. David E. Kasperowicz
May 3, 2017
Page 3 of 6

repairs and improvement contracts and services. The Board met with representatives from the management agent and, following the meeting, drafted a Memorandum of Understanding further clarifying the bidding requirements and contracting process the Board expected the management agent to follow moving forward. Yorkville never received a response from the management agent regarding the proposed Memorandum. The Memorandum as well as the cover letter sent to Yorkville's former management agent is enclosed with this response. Both documents have been redacted to remove references to specific persons and/or entities for privacy purposes. Yorkville ultimately decided not to renew its contract with its former management agent and has retained a new management agent.

Comment 1

Yorkville's position is that the prices paid for the services that were not supported by written cost estimates were, in fact, fair and reasonable. Yorkville's management agent was in the business of providing management services to various housing developments and has an office located in Northern Virginia. The management agent is experienced and is aware of the general cost of services in the area. Additionally, for the work that was contracted out prior to the management agent's relationship with Yorkville, the management agent requested proposals for the same or similar work that supported the fairness and reasonableness of the costs for services provided that were not supported by written cost estimates. Lastly, some of the services, in particular those for maintenance supplies referenced in Appendix C of the draft Audit Report, were purchased from a wholesaler that provides supplies to affordable and conventional housing nationwide. Based on the nature of this type of expense, it would be unreasonable to continuously request bids from various suppliers to provide these types of supplies.

However, as a result of this audit and their recent experience delegating responsibilities to management agents, the Board has taken steps to oversee the performance of its new management agent and to confirm that all contractor bidding requirements are met. In addition, the Board will work with their management agent to create written procedures to ensure that written cost estimates are obtained as required.

Comment 2

The second sub-finding of Finding 1 was that Yorkville's "vendors were not always properly licensed." Similar to the issue pertaining to obtaining cost estimates, Yorkville relied on its management agent to ensure that all maintenance at the property was done in accordance with applicable law. Through this audit process, it was identified that two (2) of the vendors used by Yorkville's management agent were not licensed in the Commonwealth of Virginia.

Comment 2

Yorkville believes that all work completed on the property by these vendors was done in accordance with the applicable building codes. However, Yorkville will ensure that all work was done properly and in accordance therewith. Additionally, Yorkville will work with their management agent to create written procedures to ensure that all contractors providing services to Yorkville are licensed in Virginia, as may be required by law.

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 3

Mr. David E. Kasperowicz
May 3, 2017
Page 4 of 6

The third and final sub-finding of Finding 1 was that Yorkville's "payments to vendors were not always supported" by invoices. During the stated audit period, Yorkville's management agent required conformance to strict invoicing procedures. Yorkville was required to submit invoices to the management agent, which would ensure that the invoice was uploaded to its software, prior to processing any payment. Yorkville has a list of outstanding invoices and will continue to inquire with its former management agent and its vendors for assistance in obtaining copies of the missing invoices.

Though Yorkville believes it will ultimately be able to provide copies of missing invoices to HUD, Yorkville acknowledges that it did not adequately maintain copies of invoices among its own records. To resolve that issue, Yorkville is working to develop and implement written procedures with its management agent to ensure it maintains its own record of complete documentation to support its expenditures.

Finding 2: The Cooperative Did Not Implement Recommended Corrective Actions From Our Prior Audit Report

Response:

Comment 4

Finding 2 of the draft Audit Report attributed two (2) sub-findings to Yorkville. The first such sub-finding was that Yorkville "paid for legal services that were not operating expenses." Yorkville specifically disagrees with this sub-finding of Finding 2 and states that the legal expenses were incurred on behalf of the project (as opposed to the mortgagor entity) and were reasonable and necessary in accordance with HUD Handbook 4370.2.

Comment 4

Chapter 4 of HUD Handbook 4370.2 creates a distinction between legal expenses provided on behalf of the "project" and those provided on behalf of the "mortgagor entity." Under Section 4-4 Manual of Accounts, account number 6340 explains project legal expenses as those "those incurred on behalf of the project (as distinguished from the mortgagor entity). **For example**, agents charge legal fees for eviction procedures to this account." (emphasis added). On the other hand, account number 7120 explains entity legal expenses as those "related solely to the corporation or mortgage entity." The base account number 7000 also attempts to explain the distinction between expenses incurred on behalf of the project and those incurred on behalf of the entity, stating that "[t]hese accounts record expenses applicable to the mortgagor entities distinguished from expenses **necessary and reasonable to the operation of the project**." (emphasis added).

Comment 4

The legal expenses provided to Yorkville were necessary and reasonable to the operation of the project, as opposed to on behalf of the mortgagor entity. As evidenced by the invoices issued by Yorkville's attorneys, the legal services included reviewing contracts for services provided to the community, assisting the management agent in resolving potential legal issues

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 5

Mr. David E. Kasperowicz
May 3, 2017
Page 5 of 6

involving residents, and providing advice and counsel to Yorkville's Board of Directors in the operation of the property. Additionally, Yorkville has engaged the services of an independent auditor who has reviewed Yorkville's financial reporting to ensure that it meets Government Auditing Standards. Specifically with regard to legal expenses, the 2015 audit reviewed during HUD's audit of Yorkville adjusted the entries for project and entity legal expenses. Notably, a significant portion of those expenses were identified by the independent auditor as project expenses.

Comment 6

The issue that HUD should consider is whether each legal service provided to Yorkville was necessary and reasonable to the operation of the project. The draft Audit Report suggests that this analysis has not been undertaken. In fact, the draft Audit Report states incorrectly that the "legal expense account should be used only for fees associated with rental collection." That statement is directly contradicted by the clear, unambiguous language of HUD Handbook 4370.2, which provides that rental collection is simply one example of what types of legal expenses constitute project-related legal expenses. Yorkville's legal expenses throughout the stated audit period were necessary and reasonable to the operation of the project and, therefore, are properly classified as project legal expenses. Yorkville and its attorneys remain willing to review each invoice with HUD to identify whether the legal services being provided are project or entity related.

Comment 7

The second and final sub-finding of Finding 2 was that Yorkville "did not ensure that housing assistance payments were always calculated correctly." Yorkville acknowledges that it is responsible for ensuring that its obligations under the housing assistance contract are properly followed. However, similar to the contracting issues identified in Finding 1, Yorkville's management agent was contractually obligated to ensure that the housing assistance contract was properly administered. In fact, as noted in the draft Audit Report, the management agent did not implement procedures as agreed upon to ensure that the housing assistance payment amounts were reviewed and prepared in accordance with HUD requirements.

Comment 7

As mentioned above, Yorkville selected a new management agent in September 2016. Since the new agent began working with the property, substantial changes have been made to ensure that the housing assistance contract is properly administered. Yorkville hired new staff and contracted with an experienced certification specialist to oversee the staff's training and review of Yorkville tenant files. Each of the files has been reviewed in their entirety and the certifications have been brought current. Issues in the review process have been resolved by the new staff members. Specifically regarding the eight (8) files reviewed in the draft Audit Report, Yorkville has correct those files to OIG's satisfaction and any alleged overpayments should be recaptured by HUD as the housing assistance vouchers continue to be processed.

Comment 8

Comment 7

In order to ensure that the housing assistance contract continues to be administered properly in the future, Yorkville will develop and implement procedures, with the assistance of

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

Comment 7

Mr. David E. Kasperowicz
May 3, 2017
Page 6 of 6

its management agent, to ensure that housing assistance payments are correctly calculated and supported with the required documentation. Yorkville will ensure that the procedure includes a statement from its management agent that the determined housing assistance payment amounts have been reviewed by management and were prepared in accordance with HUD requirements.

As has been illustrated through this response, Yorkville delegated many of its HUD responsibilities to its professional management agent, specifically due to the agent's sophistication and represented ability to complete tasks in accordance with HUD requirements. While Yorkville is ultimately responsible to HUD for its agent's failings, the agent should also be subject to review for its actions. Yorkville accepts its responsibility.

We hope that this response will lead you to review the conclusions that were reached during the audit process. We understand that, once the final audit is issued, we will be required to work out matters of resolution with the Baltimore field office. While the audit's findings, whether or not Yorkville agrees with them, are important, the method of resolution is more important. We at Yorkville are determined to resolve the audit in a constructive and professional manner. We hope that HUD will approach it with the same goals, so that we can continue to operate in the best interests of the property and its residents.

Sincerely



Mr. Ismail Musa
President Yorkville Board of Directors



Enclosure

Auditee Comments and OIG's Evaluation

Ref to OIG
Evaluation

Auditee Comments

[REDACTED]

[REDACTED]

[REDACTED]

July 5, 2016

[REDACTED]

RE: Yorkville Corporation – Memorandum of Understanding

Dear [REDACTED]

Please find enclosed for your review a draft memorandum of understanding we prepared in follow up to the July 17, 2016 meeting held with the Yorkville Corporation Board of Directors as well as staff members from Yorkville and [REDACTED]

As discussed during the meeting, all parties involved acknowledged communication and process issues regarding the identification of services needed for the Yorkville community, the gathering of proposals for such services, and the selection of contractors to provide the services. The enclosed memorandum of understanding we hope reflects the understandings reached among those present at the July 17th meeting. Please review the memorandum and contact us with any feedback you may have regarding the proposed processes.

We appreciate your timely and prompt consideration of this request. The Board is hopeful that preparing this written process will enable all parties to better cooperate and further the best interests of Yorkville.

If you have any questions regarding this letter, please contact our office.

Sincerely,
[REDACTED]

Enclosure
cc: Board of Directors

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation

Auditee Comments

MEMORANDUM OF UNDERSTANDING

WHEREAS, Yorkville Corporation ("Yorkville") has engaged [REDACTED] as its management agent;

WHEREAS, Yorkville and [REDACTED] identified issues of communication and process that have prevented the parties from effectively and efficiently conducting business in the best interests of Yorkville; and

WHEREAS, representatives from Yorkville and [REDACTED] met on Friday, June 17th to discuss these issues and agreed to formulate a process and procedure the parties will follow in order to ensure improved cooperation and to further the interests of Yorkville.

NOW, THEREFORE, the parties hereto set forth the following standard of practices regarding the identification of services needed, gathering proposals for such services, and selecting contractors to provide such services.

Step #1: Project Identification

Yorkville's maintenance manager shall cooperate with [REDACTED] project manager to identify projects needing to be completed at Yorkville. Both parties shall cooperate and agree on the scope of the project at hand and prepare a request for proposals ("RFP") for each project.

Step #2: Gather & Review Bids

Yorkville's maintenance manager shall submit each RFP to various contractors and shall obtain at least three (3) bids for each RFP. Upon receipt of the bids, the maintenance manager shall submit the bids to [REDACTED] project manager for review. Both the maintenance manager and the project manager shall ensure that each bid provides a detailed description of the work to be completed and the price for each service. Once all project bids have been collected and reviewed by both the maintenance manager and the project manager, both parties shall submit the bids and their recommendations to Yorkville's general manager.

Step #3: Submission to Board of Directors & Decision

If the project cost is less than \$2,500, then Yorkville's general manager shall select the contractor whose bid is in the best interests of Yorkville.

If the project cost is equal to or more than \$2,500, then Yorkville's general manager shall submit the bids and all recommendations to Yorkville's Board of Directors for their action. The bids must be provided to the Board as soon as possible, but in no event less than fifteen (15) days before the work must be scheduled. The Board shall review all bids and recommendations and select a contractor in the best interests of Yorkville. The Board may consider, among other factors, the price of the proposal, recommendations from [REDACTED] and Yorkville staff, and past experiences with the contractors.

Auditee Comments and OIG's Evaluation

Auditee Comments

Ref to OIG
Evaluation

Step #4: Attorney Review (Project cost \geq \$2,500)

Once a contractor is selected, the Board shall deliver the proposal and any contract submitted by the selected contractor to Yorkville's attorney for review. If deemed necessary, Yorkville's attorney shall draft a contract or addendum to a proposed contract to be used by Yorkville and the contractor and timely deliver it to the Board for execution.

Step #5: Payment of Invoices

In accordance with the contract, [REDACTED] shall ensure that each contractor is paid timely. However, in order to ensure prompt payment, Yorkville shall submit each invoice to [REDACTED] within three (3) business days of receipt.

In recognition of their responsibilities and obligations identified above, the parties' authorized representatives sign their names hereto.

YORKVILLE

on behalf of the Board of Directors

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

OIG Evaluation of Auditee Comments

- Comment 1 The Cooperative acknowledged its ultimate responsibility for the project's compliance with the applicable requirements, noting that it delegated responsibility for complying with applicable requirements to its management agent. It believes that the prices paid for the services that were not supported by written cost estimates were, in fact, fair and reasonable. The board has taken steps to oversee the performance of the new management agent to ensure requirements are met. It will work with the management agent to create written procedures to address the issue. We appreciate the Cooperative's acknowledgement of its responsibility for the project's compliance with applicable requirements because the Cooperative cannot delegate responsibility. We are encouraged by its statements that the board has taken steps to improve oversight over the management agent and that it will work with the management agent to create written procedures to address the issue. Although the Cooperative asserts that it paid fair and reasonable prices for the products and services questioned in the audit report, as part of the audit resolution process, it needs to provide documentation to HUD to show that it paid fair and reasonable prices for those products and services. It also needs to provide documentation to HUD to show that it developed and implemented written procedures to ensure that it obtains written cost estimates as required.
- Comment 2 The Cooperative agrees that the audit identified two vendors that were not properly licensed in the Commonwealth of Virginia and asserts that the work they completed was done in accordance with applicable building codes. It stated that it will ensure that all work was done properly in accordance with the applicable building codes. We are encouraged by the Cooperative's statement that it will ensure that all work completed by the two vendors complied with applicable building codes. As part of the audit resolution process, the Cooperative needs to provide documentation to HUD to show that the work complied with the applicable building codes.
- Comment 3 The Cooperative acknowledged that it did not adequately maintain copies of invoices in its records. It stated that it is working to develop and implement written procedures to address the issue. We appreciate the Cooperative's positive attitude. We are encouraged by its statement that it is working to develop and implement procedures to address the issue. As part of the audit resolution process, the Cooperative needs to provide documentation to HUD to support the questioned payments and to show that it developed and implemented written procedures.
- Comment 4 The Cooperative disagrees with our finding that it paid for legal services that were not operating expenses. It noted that HUD Handbook 4370.2 created a distinction between legal expenses on behalf of the project and those provided on behalf of

the mortgagor entity. It stated that the legal expenses were necessary and reasonable to the operation of the project as evidenced by the invoices for services including reviewing contracts for services provided to the community, assisting the management agent in resolving potential legal issues involving residents, and providing advice to the board regarding the operation of the property. As stated in the audit report, we found that the Cooperative paid for ineligible legal expenses associated with representation at board and community meetings and for review of business-related documents, such as proposals, contracts, membership handbooks, and documents associated with refinancing the property. None of these expenses were eligible operating expenses. The management agent should possess a sufficient level of proficiency to manage the project, handle the day to day operations, and complete tasks in accordance with HUD requirements. When the law firm provided legal advice to the Cooperative's board, it was providing legal services on behalf of the mortgagor entity because the project is a cooperative and its board is the mortgagor entity.

- Comment 5 The Cooperative stated that a significant portion of legal expenses were adjusted to project expenses by its independent auditor in its 2015 audit which HUD reviewed during its review of the Cooperative. We believe the Cooperative is referring to a review by HUD's Real Estate Assessment Center of its annual project financial information for fiscal years ended December 31, 2015, and December 31, 2014. The Center questioned unauthorized distribution of project funds for legal expenses and noted that the Cooperative is a nonprofit project and there was no surplus cash to cover entity expenses. HUD Handbook 4370.2 REV-1, CHG-1 states that corporate or mortgagor entity legal expenses require prior written approval from HUD.
- Comment 6 The Cooperative states that HUD should consider whether each legal service provided to it was necessary and reasonable to the operation of the project and the audit report suggests that this analysis had not been undertaken. It also pointed out that the language of HUD Handbook 4370.2 contradicted our statement in the audit report that "the legal expense account should be used only for fees associated with rental collection." As part of the audit resolution process, HUD will consider the Cooperative's position regarding the legal expenses. However, in two letters to the Cooperative, dated January 12, 2009, and May 7, 2009, the Director of HUD's Richmond Multifamily Division clearly clarified the difference between allowable project-based legal fees and owning entity (or mortgagor entity) legal fees. In the May 7, 2009, letter, the Director informed the Cooperative that "as a 100 percent Section 8 property the only legal fees that should be incurred and paid from operational income are fees incurred during an eviction process." Regarding the language of HUD Handbook 4370.2, we revised our statement on page 7 of the report.
- Comment 7 The Cooperative acknowledged its responsibility to ensure that it complies with its housing assistance contract. It stated that it hired new staff and contracted with

an experienced certification specialist to oversee the staff's training and review of the tenant files. Each of the files has been reviewed in its entirety, certifications have been brought current, and issues identified during the review have been resolved. The Cooperative also stated that it will develop and implement procedures to ensure that housing assistance payments are correctly calculated and supported with the required documentation, including, a statement from the management agent that it reviewed the housing assistance amounts and prepared them in accordance with HUD requirements. We appreciate the Cooperative's positive attitude. We are encouraged by its statements that it has taken action to improve its operations and that it will develop and implement procedures to address the issues. As part of the audit resolution process, the Cooperative needs to provide documentation to HUD to show that it developed and implemented sufficient written procedures.

Comment 8 The Cooperative stated that, for the eight tenant files addressed in the audit report, it corrected them to our satisfaction and that any alleged overpayments should be recaptured by HUD. We are encouraged by the Cooperative's statement that it has made the corrections in the files identified by the audit. However, the Cooperative informed us verbally of this action during the audit. It did not provide any documentation to support its verbal statement. Therefore, without any documentation to support the statement we could not and did not draw any conclusions or pass judgment on the Cooperative's corrections. As part of the audit resolution process, the Cooperative needs to provide documentation to HUD to show that it corrected the errors in the eight files identified in the audit report. The Cooperative also asserts that any alleged overpayments should be recaptured by HUD. As part of the audit resolution process, HUD will determine whether it agrees with our recommendation to direct the Cooperative to reimburse \$3,892 for the overpaid housing assistance. If HUD agrees with our recommendation, it will also determine, with our concurrence, an appropriate method of reimbursement that meets the intent of the recommendation.

Appendix C

Results of Payment Review

Seq no.	Products or services purchased	Total amount paid	Amount not supported by cost estimates	Amount paid to unlicensed vendors	Amount not supported by invoices
1	Replacement of windows and doors	\$1,140,409	\$0	\$0	\$0
2	Unit repairs	475,075	475,075	475,075	9,045
3	Heating and air conditioning repairs	425,049	421,504	0	101,741
4	Maintenance supplies	306,613	306,613	0	0
5	Legal services	296,787	0	0	0
6	Maintenance	250,663	170,688	250,663	0
7	Unit Repairs	247,301	247,301	0	0
8	Management agent fees	220,483	0	0	0
9	Health insurance	158,799	0	0	0
10	Unit repairs	149,803	149,803	0	53,099
	Totals	3,670,982	1,770,984	725,738	163,885