



# Diamond Park, Philadelphia, PA

## HUD-Insured Section 202 Multifamily Rental Housing for Seniors and Persons With Disabilities



**To:** Brenda J. Brown, Director, Asset Management Division, Baltimore Satellite Office, Multifamily Northeast Region, 3BHMLAP  
**//signed//**

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

**Subject:** The Owner of Diamond Park, Philadelphia, PA, Generally Managed Its HUD-Insured Property in Accordance With 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 HUD-insured Diamond Park multifamily project.

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: 2018-PH-1004**

**Date: May 1, 2018**

**The Owner of Diamond Park, Philadelphia, PA, Generally Managed Its HUD-Insured Property in Accordance With Applicable Requirements**

## Highlights

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### What We Audited and Why

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We audited Diamond Park because of concerns raised by the U.S. Department of Housing and Urban Development's (HUD) Departmental Enforcement Center regarding the management of the project and we had never audited it. Our audit objective was to determine whether the owner managed the project in accordance with its regulatory agreement and HUD requirements. We focused the audit on reviewing (1) participant eligibility and their selection from the waiting list; (2) the accuracy of and support for housing assistance payments; (3) the management of security deposits and rental receipts; (4) the use of operating funds; (5) the management and use of reserve for replacement funds; (6) maintenance of the property; (7) whether the project made mortgage payments; and (8) whether the project submitted annual financial statements.

### What We Found

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The owner of Diamond Park generally managed its project in accordance with its regulatory agreement and HUD requirements. Specifically, the owner (1) assisted eligible participants; (2) made housing assistance payments that were generally accurately calculated, and supported; (3) properly managed its security deposits and rental receipts; (4) properly used operating funds; (5) properly managed and used reserve for replacement funds; (6) maintained the property in good physical condition; and (7) made mortgage payments as required. However, it did not maintain adequate documentation to show that participants were selected from its waiting list as required and did not submit financial statements for fiscal years 2013 through 2016. These conditions occurred because the project lacked procedures to ensure that it maintained documentation to show that it selected participants from the waiting list appropriately and lacked funds to pay an independent accounting firm to audit its financial statements. As a result, HUD had no assurance that the project treated applicants fairly and consistently in accordance with program requirements and was unaware of the project's financial position. During the audit, HUD began working with the owner to have an independent accounting firm prepare the missing financial statements.

### What We Recommend

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We recommend that HUD require the owner to develop and implement procedures to ensure that it maintains documentation to show that it selected participants from the waiting list in accordance with applicable requirements. We did not make a recommendation regarding the missing financial statements because HUD was working with the owner to correct the situation.

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# Background and Objective

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Diamond Park opened in 1985. The project is owned by Partnership for Urban Housing Development, Inc. The owner entity was incorporated under the nonprofit corporation law of the Commonwealth of Pennsylvania on May 31, 1978. The project is governed by a nine-member board of directors. Proficient Management Services has been the management agent of the project since September 2013. Diamond Park has a total of 48 housing units, all located in Philadelphia, PA, at 2 different locations that are a few blocks apart. Twenty-four units are located at 1700 West Susquehanna Avenue, and 24 units are located at 1500 West Page Street. The U.S. Department of Housing and Urban Development's (HUD) Multifamily Northeast Region Asset Management Division located in Baltimore, MD, has oversight responsibility for the project. The project receives project-based Section 8 assistance for 47 of its 48 housing units available to seniors and persons with disabilities. HUD has provided the following housing assistance over the last 3 years.

Year	HUD project-based housing assistance
2016	\$566,746
2015	562,907
2014	567,649
<b>Total</b>	<b>1,697,302</b>

The project's mortgage was insured by the Federal Housing Administration (FHA) under Section 202<sup>1</sup> of the Housing Act of 1959. In January 2009, the owner refinanced the mortgage under Section 207, according to Section 223(f) of the National Housing Act.<sup>2</sup> HUD governs the loan through a regulatory agreement with the owner. As of December 2017, the project's mortgage was current, and the remaining balance of the mortgage totaled more than \$2.5 million.

HUD's Departmental Enforcement Center raised concerns to us regarding the management of the project, including its failure to submit annual financial statements for fiscal years 2013 to 2015.

Our audit objective was to determine whether the owner managed the project in accordance with its regulatory agreement and HUD requirements. We focused our work on reviewing (1) participant eligibility and their selection from the waiting list; (2) the accuracy of and support for housing assistance payments; (3) the management of security deposits and rental receipts; (4) the use of operating funds; (5) the management and use of reserve for replacement funds; (6) maintenance of the property; (7) whether the project made mortgage payments; and (8) whether the project submitted annual financial statements.

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<sup>1</sup> Until the creation of the Section 811 program in 1990, the Section 202 program provided funding to nonprofit organizations that developed and operated housing for seniors with very low incomes and people with disabilities.

<sup>2</sup> Section 207-223(f) insures mortgage loans to facilitate the purchase or refinancing of existing multifamily rental housing. These projects may have been financed originally with conventional or FHA-insured mortgages.

# Results of Audit

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## **Finding: The Owner of Diamond Park Generally Managed Its Project in Accordance With Applicable Requirements**

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The owner generally managed the project in accordance with its regulatory agreement and HUD requirements. Specifically, the owner (1) assisted eligible participants; (2) made housing assistance payments that were generally accurately calculated, and supported; (3) properly managed its security deposits and rental receipts; (4) properly used operating funds; (5) properly managed and used reserve for replacement funds; (6) maintained the property in good physical condition; and (7) made mortgage payments as required. However, it did not maintain adequate documentation to show that it selected participants from its waiting list as required and did not submit financial statements for fiscal years 2013 through 2016. These conditions occurred because the project lacked procedures to ensure that it maintained documentation to show that it selected participants from its waiting list appropriately and the project lacked funds to pay an independent accounting firm to audit its financial statements. As a result, HUD had no assurance that the project treated applicants fairly and consistently in accordance with program requirements and was unaware of the project's financial position.

### **Participants Met Eligibility Requirements**

Our review of the files for the four participants most recently admitted into the project contained documentation to show that they were eligible for assistance. The files contained documentation, such as Social Security documentation, income documentation, criminal background checks, and citizenship documentation. We also screened the Social Security numbers of the participants and household members who lived at the project from August 2015 through September 2017 and found that the project did not make assistance payments on behalf of persons who were deceased. From this review, we noted that as a best practice, the project should maintain the criminal background checks in a separate, secure file.

### **The Project Made Housing Assistance Payments That Were Generally Accurately Calculated, and Supported**

For the same four participants discussed in the paragraph above, the project generally accurately calculated their housing assistance payments. For one of the participants, the project made a minor error that resulted in an immaterial difference in the housing assistance payment. We discussed the error with the owner so that the necessary corrections could be made. All four files contained documentation, such as income and asset verifications, declaration of non-employment forms, and reports from HUD's Enterprise Income Verification system,<sup>3</sup> to support the payments.

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<sup>3</sup> The Enterprise Income Verification system is a web-based computer system that contains employment and income information of individuals who participate in HUD rental assistance programs.

### **The Project Complied With Security Deposit Requirements**

The regulatory agreement required the project to collect from new participants a security deposit equal to 1 month's rent and place security deposits into a separate bank account. The lease agreement required the project to refund the security deposits to participants who provided a 30-day written notice of intent to move. We reviewed the security deposits for the four participants most recently admitted into the project and the security deposit refunds for the last six participants who moved out. The project maintained documentation, such as bank statements, lease agreements, copies of checks, and 30-day written notices from participants, to show that it complied with the requirements.

### **The Project Properly Deposited Rental Receipts as Required**

The regulatory agreement required the project to deposit all rents into a financial institution. For July 2017, the project collected rents totaling \$8,323. The project maintained documentation, such as a bank statement and copies of checks, to show that it properly deposited the rents as required.

### **The Project Used Operating Funds as Required**

Section 2-6 of HUD Handbook 4370.2, REV-1, required that only reasonable and necessary expenses be charged to the project. We reviewed 87 payments of operating funds totaling \$151,819 and determined that the project maintained documentation, such as a management agreement, invoices, bank statements, copies of checks, and payroll records, to show that the payments were reasonable, necessary, and supported.

### **The Project Established, Maintained, and Used Its Replacement Reserve Funds as Required**

The regulatory agreement required the project to establish and maintain a reserve for replacement fund in a separate bank account and deposit \$1,600 per month into it.<sup>4</sup> The project maintained bank statements to show that it had established the account and that it made the required monthly deposits. The balance in the account as of December 2017 was \$152,003.

The project used its reserve for replacement funds as required. Regulations at 24 CFR (Code of Federal Regulations) 891.405 required HUD to approve the use of the funds before the project drew them from the account. From August 2015 through July 2017, the project made only one draw from this account. In November 2016, it made a \$4,315 draw to replace the emergency call system. The project had documentation, such as a HUD-approved funds authorization form, a contractor proposal, and an invoice, to support the draw.

### **The Project Maintained the Property in Good Physical Condition**

HUD's Real Estate Assessment Center performed its most recent physical inspection of the project buildings and apartments in January 2017 and gave the project a score of 98b.<sup>5</sup> During a

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<sup>4</sup> Reserve for replacement funds are generally used to replace a project's capital items or for emergency purposes.

<sup>5</sup> A passing score is 60 or higher. The score determines the timeline for the project's next inspection. A score of 90 or higher means that the property's next routine inspection should be in 3 years. The letter "b" indicated that the inspector noted non-life-threatening health and safety deficiencies.

physical tour of the project, we observed that the buildings and apartments were in good condition.

### **The Project Made Mortgage Payments as Required**

The regulatory agreement required the project to make all payments due in accordance with the mortgage note. The mortgage note stated that payments of principal and interest in the amount of \$20,440 were due and payable monthly. HUD's Multifamily Default and Delinquency Reporting report and the project's cash disbursement register showed that the project was current on its mortgage.

### **The Project Did Not Maintain Adequate Documentation To Show That It Selected Participants From Its Waiting List in Order**

HUD Handbook 4350.3, REV-1, section 4-18, required the project to develop a method to maintain documentation of the waiting list composition, application status, and actions taken. Section 4-23 required the project to select the next applicant from its waiting list when a unit became vacant. The project did not maintain adequate documentation to show that it selected the four participants that were most recently admitted to the project from its waiting list in the order of their application. This condition occurred because the project lacked procedures to ensure that it maintained documentation to show that it selected participants from the waiting list in order. The project used a computer program to maintain its waiting list and the program did not have the capability to recreate waiting lists for dates in the past. As a result, HUD had no assurance that the project treated applicants fairly and consistently in accordance with program requirements.

### **The Owner Did Not Submit the Project's Financial Statements as Required**

The regulatory agreement required the owner to submit annual audited financial statements. Regulations at 24 CFR 5.801 required the owner to submit annual audited financial statements no later than 90 days after the end of its fiscal year.<sup>6</sup> For fiscal years 2013 through 2016, the owner did not submit audited financial statements for the project as required. This condition occurred because the project lacked funds to pay an independent accounting firm to audit its financial statements. The project's fiscal year 2012 audited financial statements showed that the operating account had an ending balance of \$17,273 and a surplus cash deficiency of \$76,240. The project owner estimated that it would cost \$21,000 for an independent accounting firm to audit its financial statements for fiscal year 2013. We reviewed the project's cash disbursement register for the period August 2015 through July 2017, and it showed that the project operated at a loss of \$8,765. As of December 2017, the project's operating account had an ending balance of \$7,798. As a result, because the project did not submit audited financial statements, HUD was unaware of the project's financial position.

In October 2017, the owner requested that HUD allow it to use its reserve for replacement funds to hire an independent accounting firm to audit its financial statements for fiscal year 2013. As of February 2018, HUD had approved the owner to use nearly \$20,000 of its reserve for replacement funds to hire an independent accounting firm to prepare its audited financial

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<sup>6</sup> Diamond Park's fiscal year begins January 1 and ends December 31.

statements for fiscal year 2013. HUD stated that after the fiscal year 2013 audited financial statements were completed, it would work with the project on providing approval to use its reserve for replacement funds to prepare audited financial statements for fiscal years 2014 and beyond. Since HUD was working with the owner to correct this situation, we did not recommend any further action.

### **Conclusion**

The owner of Diamond Park generally managed its project in accordance with its regulatory agreement and HUD requirements. The conditions identified by the audit occurred because the project lacked procedures to ensure that it maintained documentation to show that it selected participants from its waiting list in the order of their application and lacked funds to pay an independent accounting firm to audit its financial statements. As a result, HUD had no assurance that the project treated applicants fairly and consistently in accordance with program requirements and was unaware of the project's financial position. Since HUD was working with the owner to have an independent accounting firm prepare the missing financial statements, we did not make a recommendation.

### **Recommendations**

We recommend that the Director of HUD's Asset Management Division, Baltimore Satellite Office, Multifamily Northeast Region, require the owner to

- 1A. Develop and implement procedures to ensure that it maintains documentation to show that it selected participants from its waiting list in accordance with applicable requirements.
- 1B. Develop and implement procedures to ensure that it maintains criminal background checks in separate, secure files.

# Scope and Methodology

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We conducted the audit from August 2017 through March 2018 at Diamond Park's office located at 1700 West Susquehanna Avenue, Philadelphia, PA, and at our office located in Philadelphia, PA. The audit covered the period April 2014 through September 2017 but was expanded to include the periods January through December 2013 and September 2017 through February 2018 since the owner did not submit annual audited financial statements during these periods.

To accomplish our objective, we reviewed

- HUD's program requirements at 24 CFR Parts 891 and 5, HUD Handbooks 4350.3 and 4370.2, the housing assistance payment agreement, the regulatory and use agreement, the mortgage note, the management certification, and HUD's income limits.
- The project's audited financial statement for fiscal year 2012 and its organizational chart.
- The project's cash disbursement register, general ledger, invoices, payroll registers, participant files, rent roll report, rent schedules, waiting list, and bank statements.
- HUD's April 2017 management and occupancy review report.
- The project's policies and procedures handbook related to applicant eligibility, waiting list administration, security deposits, and rent collection.

We observed the physical condition of the project buildings and two apartments to determine whether the project was maintained in good condition. We interviewed officials and employees of the project and HUD staff.

To achieve our audit objective, we relied in part on computer-processed data from the project's computer system. We used information from the project's cash disbursement register to identify vendors with the largest disbursements during the period August 2015 through July 2017. We also used the project's rent roll report as of August 2017 to identify participants that were most recently admitted to the project. 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. The testing entailed comparing the project's cash disbursement register to bank statements and the project's rent roll report to the participant files.

We reviewed a nonstatistical sample of 4 participant files from a universe of 45 participants that the project assisted as of August 2017. These four participants were the most recent participants admitted into the project. Three were admitted in 2017, and one was admitted in 2014. We reviewed the files to determine whether the participants met eligibility requirements and the project accurately calculated housing assistance payments and maintained documentation to

support the calculations, properly selected participants from its waiting list, and collected the correct security deposit amounts. We also reviewed security deposit refunds the project made for six participants who moved out during the period April 2014 through August 2017 to determine whether the project refunded the correct security deposit amounts to them.

We screened the Social Security numbers for 55 participants and household members who lived at the project during the period August 2015 through September 2017 to determine whether the project made payments for any persons who were deceased.

We selected a sample of 87 payments totaling \$151,819 from a list of 722 payments totaling \$1.4 million that the project made using operating funds during the period August 2015 through July 2017. We selected the 87 payments because they represented the largest payments, excluding all routine payments for expenses such as utilities and mortgage payments.

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

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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 objective:

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.
- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.
- Compliance with applicable laws and regulations – Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.

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.

We evaluated internal controls related to the audit objective in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance regarding the effectiveness of the internal control structure as a whole. Accordingly, we do not express an opinion on the effectiveness of Diamond Park's internal control.

# Appendix

## Appendix A

### Auditee Comments and OIG's Evaluation

#### Ref to OIG Evaluation

#### Auditee Comments

Comment 1

Comment 2

**DIAMOND PARK**

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1700 W. Susquehanna Ave. Box 17  
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March 28, 2018

Philadelphia, Pa. 19121-1622  
(215) 765-6626

Mr. David Kasperowicz  
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Regional Inspector General for Audit  
Philadelphia Regional Office, 3AGA  
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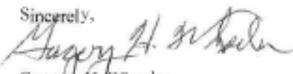
Dear Mr. Kasperowicz:

I am writing to respond to your report on Diamond Park Apartments and to specifically address your recommendation and findings. We have two basic comments, one addressing the lone recommendation made. The second dealing with your representation concerning HUD's knowledge regarding our financial position.

**Comment I:** Regarding maintenance of documentation that tenant participants were selected from the waiting list in accordance with applicable requirements.

Ownership and management have already instituted new procedures to adequately document tenant selection procedures from the waiting list. Management is further reassessing computer programs used to manage the waiting list, the selection there from, and waiting list(s) updates to assure that this can be accomplished and maintained electronically in the future.

**Comment II:** As to the representation on (page 6) stating that HUD was unaware of the precarious nature of our financial position, due to the lack of annual audited statements being submitted since 2013; since 2011 when HUD substantially cut our contract rents, they were well aware of our financial position having received monthly financial reports from our three management agents during that time.

Sincerely,  
  
Gregory H. Wheeler  
President

Cc: Ronald Lloyd, Assistant Regional Inspector General for Audit

Partnership for Urban Housing Development, Inc.

## OIG Evaluation of Auditee Comments

- Comment 1 The owner stated that ownership and management had already instituted new procedures to adequately document tenant selection procedures from the waiting list. The owner also stated that management was reassessing computer programs used to manage the waiting list, including applicant selection. We did not review the new procedures cited by the owner. However, as part of the audit resolution process, HUD will evaluate the owner's corrective actions to ensure that they satisfy the recommendation.
- Comment 2 The owner stated that HUD was aware of the project's financial position because its management agents submitted monthly financial reports to HUD. Although the agents may have submitted monthly reports for establishing net income<sup>7</sup> to HUD, those self-certified reports provided information for only part of the project's financial operations. It did not include a statement of financial position, the related statements of activities, changes in net assets, and cash flows, and any notes to the financial statements. The regulatory agreement required a certified public accountant to prepare and certify the project's annual financial statements. A certified public accountant is responsible for expressing an opinion on the project's financial statements, including the financial position of the project and changes in its net assets and cash flows. As stated in the audit report, HUD had approved the owner to use nearly \$20,000 of its reserve for replacement funds to hire an independent accounting firm to prepare its audited financial statements for fiscal year 2013. HUD stated that after the fiscal year 2013 audited financial statements were completed, it would work with the project on providing approval to use its reserve for replacement funds to prepare audited financial statements for fiscal years 2014 and beyond. Since HUD was working with the owner to correct this situation, we did not recommend any further action.

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<sup>7</sup> Form HUD-93479