



UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

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RESOURCES AND ECONOMIC  
DEVELOPMENT DIVISION

July 3, 1975

The Honorable H. R. Crawford  
Assistant Secretary for Housing Management  
Department of Housing and Urban Development

Dear Mr. Crawford:

The General Accounting Office is reviewing HUD's use of independent public accountants (IPAs) to audit local housing authorities (LHAs). We believe that HUD needs to strengthen its procedures and practices for making special audit subsidy payments to LHAs. Specifically, HUD needs to (1) insure that LHAs properly allocate audit costs between development and management activities and that audit subsidies not be used to pay audit costs charged to development costs, and (2) revise its procedures so that special audit subsidy payments are based on actual rather than estimated costs.

We examined audit subsidies totaling \$82,498, which were provided to 30 LHAs who are undertaking housing development projects in eight HUD regions--Atlanta, Boston, Dallas, Chicago, Denver, Kansas City, New York, and San Francisco. We found that audit subsidy overpayments of \$11,164 have been made to 16 of the 30 LHAs. In addition, an undetermined amount of overpayments may be made to 13 LHAs (including 5 of the 16) because they did not allocate a portion of the audit costs to housing development activities. If these costs are subsequently allocated to development costs, as required by HUD regulations, a double payment will occur.

Our observations on these matters follow.

BACKGROUND

Prior to 1972, HUD audited LHAs without charge. In July 1972, a housing management circular directed each LHA, with 5,000 housing units or less, to engage an IPA to audit its financial statements biennially. LHAs are to obtain proposals from at least three IPAs, select the best proposal, and submit it to the HUD regional inspector general for audit (RIGA) for concurrence. Upon completion of the audit, the IPA submits copies of his report to the RIGA for review and approval. After approval the LHA is authorized to pay the IPA. In those cases where an IPA audit covers development and management activities, each LHA is required to allocate the audit fee between the two activities. Development funds are to be used to pay for audit fees charged to development and management funds, including special audit subsidies, are to be used to pay audit fees charged to management activities.

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There are about 2,600 LHAs which contract with IPAs for about 1,300 audits annually. LHAs were required initially to pay IPAs for these audits which cost about \$3 million annually.

During 1974, HUD began reimbursing some LHAs for the portion of their IPA audit costs allocated to management because HUD's procedures for computing operating subsidies to LHAs did not consider audit costs. On May 23, 1974, you directed HUD regional offices to allocate \$5 million for a special additional operating subsidy to pay LHAs for audit costs they incurred during 1973 and 1974.

To qualify for an audit subsidy the LHAs must meet certain requirements. The audit cost must be included in the LHA's budget which is approved by HUD and the budget must not show that the LHA would owe HUD money as a result of income earned. The audit subsidy is added to any regular operating subsidy which the LHA would receive from HUD.

In April 1975 HUD initiated a new performance funding system for allocating operating subsidies to LHAs. Under this system, HUD will pay LHAs, in addition to any regular operating subsidy, an audit subsidy for the estimated costs of IPA audits chargeable to management, if the LHA's operating budget forecasts a deficit.

#### RESULTS OF REVIEW

Our review showed that 11 LHAs under the jurisdiction of the HUD Dallas Regional Office, received subsidies for audit costs totaling \$17,067, of which \$9,704 was charged to development costs. Allowable costs, such as audit costs, which are charged to development are paid by HUD through the separate development advances it provides LHAs. Therefore, the \$9,704 was paid by HUD twice--through audit subsidies and development advances. See appendix 1 for the details of these 11 cases.

Our review also showed that 7 LHAs (including 2 of the 11) under the jurisdiction of four HUD Regional Offices--Atlanta, Dallas, Denver, and Chicago--received audit subsidies in excess of the actual IPA audit fees by \$1,460. Appendix I also contains the details on these overpayments.

Our review further showed that 13 LHAs (including 5 of the 7) in 5 HUD regions--Atlanta, Boston, Chicago, Denver, and New York--had development activities during the audit period, but none of these authorities had allocated any audit costs to development. As stated previously, HUD regulations require such an allocation when housing development is in process. Therefore, during the next audit of these LHAs, the IPAs should reclassify part of the prior audit costs as development costs. If this occurs, HUD will pay twice for the portion reclassified as development costs. See appendix II for a listing of these LHAs.

HUD area office officials told us that overpayments occur because they approve audit subsidies during the LHA's budgeting process which generally occurs prior to LHA's contracting with an IPA for an audit. The area office officials often have no way of knowing at the time of the budgeting process what the actual audit fee will be or what portion will be charged to development. Area office and headquarters housing management officials told us that there are no HUD procedures requiring that audit subsidy payments be reconciled with actual audit costs or charges made to development.

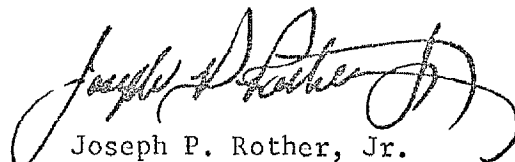
#### CONCLUSIONS AND RECOMMENDATIONS

We believe HUD instructions should be revised to require that audit subsidies be paid to LHAs only on the basis of actual audit costs and after a determination is made by the LHA and approved by HUD as to how much of the audit costs will be charged to development activities. Accordingly, we recommend that you:

- establish, in conjunction with the Inspector General, procedures requiring (1) LHAs to inform RIGAs of their allocation of the proposed audit fees between development and management activities at the time LHAs submit selected audit proposals to the RIGAs, (2) RIGAs to review the allocations and inform the LHAs and area offices of their determinations, and (3) area offices to pay audit subsidies to LHAs only after they have received the RIGA's allocation determinations so that audit subsidies are paid for only the actual costs chargeable to management;
- require that HUD regional offices (1) review each audit subsidy approved to date to determine whether the subsidy is in excess of the actual audit cost incurred by the LHA and whether an overpayment for audit costs will occur if audit costs improperly charged to LHA operations are subsequently reclassified as development costs, and (2) take action to collect or prevent any overpayment; and
- require that HUD regional offices take action to (1) collect the \$11,164 which was overpaid to the 16 LHAs listed in appendix I and (2) prevent overpayments to the 13 LHAs listed in appendix II.

We would be pleased to discuss with you or members of your staff the above matters and would appreciate your comments on any action taken or planned. Copies of this letter are being provided to the Assistant Secretary for Housing Production and Mortgage Credit and the Inspector General.

Sincerely yours,

  
Joseph P. Rother, Jr.  
Assistant Director

LHAS WHICH RECEIVED EXCESSIVE  
SUBSIDIES FOR AUDIT COSTS

<u>LHAS</u>	<u>Audit subsidies received</u>	<u>IPA audit fees</u>	<u>Charges to develop- ment costs</u>	<u>Audit fees paid twice</u>	<u>Subsidies in excess of audit fees</u>
Walsenburg, Colorado	\$ 1,440	\$ 1,400	-	-	\$ 40
Sarasota, Florida	9,500	9,250	-	-	250
Randolph County, Illinois	5,000	4,125	-	-	875
Independence, Louisiana	1,772	1,772	\$ 988	\$ 988	-
Minot, North Dakota	2,500	2,440	-	-	60
Elk City, Oklahoma	1,493	1,493	886	886	-
Tichomingo, Oklahoma	1,200	1,365	965	800	-
Austin, Texas	2,970	2,970	2,100	2,100	-
Carrizo Springs, Texas	1,200	1,125	450	450	75
Gatesville, Texas	1,585	1,500	1,000	1,000	85
Lott, Texas	1,365	1,365	739	739	-
Luling, Texas	1,760	1,760	760	760	-
Maud, Texas	1,200	1,230	600	570	-
San Saba, Texas	1,253	1,253	975	975	-
Schulenburg, Texas	1,269	1,269	436	436	-
Greenwood, Wisconsin	800	725	-	-	75
<b>Total</b>	<u>\$36,307</u>	<u>\$35,042</u>	<u>\$9,899</u>	<u>\$9,704</u>	<u>\$1,460</u>
<b>Total overpayments</b>					<u>9,704</u> <u>\$11,164</u>

LHAs WHOSE AUDIT COSTS SHOULD  
BE PARTIALLY ALLOCATED TO DEVELOPMENT

<u>LHAs</u>	<u>Audit subsidies received</u>	<u>IPA audit fees</u>
Boulder, Colorado	\$ 3,250	\$ 3,250
Walsenburg, Colorado	1,440	1,400
Sarasota, Florida	9,500	9,250
Randolph County, Illinois	5,000	4,125
Lowell, Massachusetts	5,600	5,600
North Adams, Massachusetts	3,500	3,500
Bridgeton, New Jersey	2,560	2,560
Elizabeth, New Jersey	4,800	4,800
Salem, New Jersey	2,560	2,560
Trenton, New Jersey	4,200	4,200
Woodbridge, New Jersey	1,650	1,650
Minot, North Dakota	2,500	2,440
Greenwood, Wisconsin	<u>800</u>	<u>725</u>
Total	<u>\$47,360</u>	<u>\$46,060</u>