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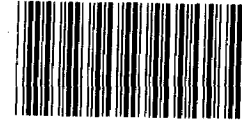


UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

April 28, 1980

COMMUNITY AND ECONOMIC  
DEVELOPMENT DIVISION

B-198505



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The Honorable Bennett M. Stewart  
House of Representatives

Dear Mr. Stewart:

Subject: The Chicago Housing Authority Needs to Improve its Management and Controls Over Purchasing (CED-80-93)

DL600908

In response to your November 1, 1979, letter and discussions with your office, we surveyed the controls the Chicago Housing Authority (CHA) exercises over its procurement of goods and services. As agreed, we did not address the elevator maintenance contract because of a current investigation by the U.S. attorney.

CHA needs to improve its management and controls over purchasing to ensure efficient and economical purchasing and guard against possible fraud. Although CHA's purchasing policies appear adequate on the surface, the CHA staff readily circumvented these policies. Controls designed to ensure free and open competition for large purchases are avoided through the use of order splitting and open purchase orders. Also, purchasing methods allowing project management personnel to make small or urgent purchases quickly are being abused.

In addition, basic procurement management information, such as total purchases by vendor or by category, is not readily available at CHA. The accounting system is such that even total purchases can only be estimated. Requirement planning, important to purchasing management, is not systematically carried out because the needed information, although prepared, is inadequately disseminated.

CHA's Executive Director agreed with our findings and said that management practices would be tightened to control the use of open purchase orders, charge accounts, and confirming purchase orders. Also, detailed budget material listings will be used to consolidate purchases and award contracts.

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The Department of Housing and Urban Development (HUD), which currently provides about two-thirds of CHA's operating budget, has not adequately reviewed and monitored CHA operations. Although required to do so every 6 years, until this year HUD had not comprehensively reviewed CHA management since 1962.

CHA is a major Chicago landlord, housing 140,000 people in the 40,000 rental units it owns and/or manages under various Federal housing programs. Policy is set by the Board of Commissioners and carried out by an Executive Director and his staff. CHA employed 2,400 people and spent over \$100 million operating its properties in 1979. HUD subsidizes rental operations and in 1979 provided about \$56 million in subsidies.

CHA has been operating at a deficit since 1977 and continues to stay solvent only because HUD had paid advance subsidies totaling \$20 million through 1979. The deficit has grown from \$7.2 million at December 31, 1977, to \$23.1 million at December 31, 1979, and the 1980 budget projects an additional deficit of \$20 million. CHA's Executive Director believes that unless HUD is able to provide additional funds, CHA will be insolvent by July 1980.

In recognition of this problem at CHA and other public housing authorities, HUD, in its fiscal year 1981 budget estimates, is proposing a one time \$52.6 million supplemental appropriation for fiscal year 1980. The supplemental appropriation is intended to provide additional payments to 10 housing authorities across the Nation for which tenant income combined with the subsidy provided under the Performance Funding System and available operating reserves has been inadequate to meet current operating expenses. The Performance Funding System was designed to provide the operating subsidy required to effectively operate a well-managed housing authority.

#### PURCHASING POLICIES CIRCUMVENTED

CHA purchasing policies follow the theory of free competition. In general, procurements over \$5,000 must be awarded by contract after sealed bids are submitted. Purchases over \$10,000 must be publicly advertised and approved by the Board of Commissioners before the contract is awarded. Purchases under \$5,000 can be made through purchase orders after informal price solicitations. Purchases under \$100 can be made by project personnel using charge accounts or petty cash. The Board of Commissioners requires monthly reports on all contracts over \$5,000 it has not approved and all purchases over \$2,500 resulting from sole-source solicitations.

These purchasing controls and policies, however, have been consistently circumvented. To avoid the Board's reporting requirements and competitive bid procedures, CHA officials have employed split purchases, open-ended purchase orders, and uncontrolled use of charge accounts and confirming purchase orders.

### Split purchases

CHA has not defined what constitutes a single procurement action. Thus, personnel have split large purchases into several orders to avoid the reporting and bidding requirements. For example:

--Eight months of water treatment service was requested by project personnel, who also suggested a sole-source supplier. After determining that the total cost would be \$3,400, officials revised the service period to 4 months and processed a purchase order for \$1,700 to the suggested sole source. In addition, two subsequent requisitions, each for 4 months of service, were processed for amounts of \$1,704 and \$1,700, respectively. The total of the three separate purchases was \$5,104.

--Four requisitions were prepared within 3 days for 800 pails of rat poison. The total cost of the purchases was \$9,200. Quotes were received from three vendors, and four purchase orders for \$2,300 each were issued.

--Four purchase requisitions were prepared the same day for the same type of heating repairs at two locations. The total cost of the work was estimated to be \$8,800. After requesting quotations from three vendors and receiving responses from two, CHA personnel issued four \$2,100 purchase orders totaling \$8,400.

CHA personnel kept these purchases below the \$2,500 and \$5,000 limits and so avoided formal bidding and the commissioners' scrutiny.

### Open purchase orders

During 1979, 153 open purchase orders were issued to 26 vendors for miscellaneous materials and repair parts. The total value of these purchase orders for various materials needed by the central maintenance division was \$365,000, with 149 marked "not to exceed \$2,400." Ten vendors received purchase orders totaling over \$10,000, with the two largest receiving \$60,000 and \$48,000.

Various items were purchased as needed. According to CHA's Executive Director, one open order was used to acquire seven or eight \$5,000 welding machines under a lease-purchase agreement. These probably would not have been approved had they been requested in the budget, this official said.

According to CHA's Purchasing Agent, the use of these open orders was not formally authorized by the Board of Commissioners. Both the commissioners' reporting and approval process and the formal bid requirements were circumvented.

Charge accounts

CHA procedures allow development managers to make purchases of \$100 or less with charge accounts. These purchases are to be limited to infrequently used or emergency items and are not to be used when it is possible to anticipate needs and order in large quantities through more formal purchasing procedures.

The use of charge accounts at CHA has not been adequately controlled. CHA management does not monitor their use or know of the total amount of charge account activity. Although CHA does not keep records of the 17 active charge accounts, a special purchasing department study found that charge purchases from three vendors totaled \$664,000 in 1979. One vendor, a hardware supplier, had charges that year of \$421,000. Some projects were either placing daily orders or were purchasing more than \$100 in goods at a time. Their purchases totaled as follows.

<u>Project office</u>	<u>1979 Charge purchases</u>
Washington Park	\$ 55,034
Ickes	49,066
Abla	37,134

If all these purchases were for orders of \$100 or less, they had to be made at a rate of more than one a day.

Although CHA officials have been aware of charge account abuse for several years, they have done little to end it. In June 1978 CHA's Director of Management rebuked project personnel for abusing one of the charge accounts by ordering hardware day by day instead of through normal purchasing channels. As the Director stated, charge purchasing was more expensive than other purchasing methods.

Confirming purchase orders

With verbal approval from headquarters, project personnel can issue confirming purchase orders to obtain goods and services costing more than \$100. These confirming orders, issued without going through the normal purchasing process, are supposed to be used for urgently needed items or to continue work in process.

CHA personnel have been abusing the use of confirming purchase orders, using them for daily business rather than for urgent situations. In 1978 CHA's external auditors found that confirming purchase orders were used for ordinary purchases and that items were ordered or purchased before headquarters' verbal approval was received. In 1979 this practice continued as CHA issued 2,583 confirming purchase orders in addition to the 4,857 regular purchase orders issued during that year.

Many of the confirming purchase orders we reviewed were used to conduct day-to-day operations rather than to meet emergencies. For example, seven management organizations used confirming purchase orders to pay photocopier rental charges. Confirming purchase orders were also used to pay for conferences at the University of Chicago, gasoline, bus rental for a day care program, and recurring rental of radio equipment in addition to items that did appear to be valid emergencies.

MANAGEMENT INFORMATION NOT AVAILABLE

Information needed to manage CHA procurement of goods and services is not readily available. CHA does not know how much money it spent purchasing what goods and services from whom or where they were obtained. CHA's Executive Director estimated that CHA spent \$20-22 million to purchase goods and services in 1979.

The purchasing department is primarily responsible for acquiring goods and services at using departments' requests. The fiscal department is responsible for processing payments to vendors. Although these two departments exchange some information, neither has full information on purchases.

The purchasing department keeps purchase order records by vendor and type of procurement, a contract log showing the value of all contracts awarded, and records of confirming purchase orders. In addition, it reports monthly on the number but not the value of purchase orders and confirming purchase orders prepared. It maintains no formal records of charge account purchases.

The fiscal department records disbursements, unfilled purchase orders, and uncompleted contracts. However, the accounting system was not designed to retrieve such information as total purchases by vendor, by category of goods and services, or by method of purchase. In fact, it is extremely difficult to track a purchase order through the system to determine when the merchandise was received and paid for.

Information to plan procurements not used

CHA is not using available information to consolidate purchases. Consolidation would result in more efficient and economical purchasing by taking advantage of quantity discounts and competition.

CHA has awarded annual contracts for a number of requirements, including window glass, toilet seats, refrigeration compressors, lock sets, and wiping rags. These contracts allow it to obtain a better price for items because annual needs are determined and formal bids are obtained for meeting them. Although CHA has not systematically evaluated its purchases to determine whether additional requirement contracts could be awarded, the purchasing department occasionally discovers items suitable for such contracts.

For example, in March 1979 the purchasing department noted that CHA wrote purchase orders for 410 automotive batteries between December 26, 1975, and August 21, 1978. This worked out to 1-1/2 batteries per vehicle per year. In addition, between January 1, 1979, and March 15, 1979, CHA purchased 111 batteries using confirming purchase orders, more than 1-1/4 batteries per vehicle in just 2-1/2 months. Based upon this information, CHA instituted controls and in January 1980 awarded a contract for automotive batteries.

Information is available to allow CHA to systematically forecast its requirements and make better use of contracts. During annual budgeting, project managers estimate their detailed needs for all materials for the upcoming year. According to a CHA Budget Officer, this information has long been available but no one has ever requested it. Purchasing officials were unaware the information existed but thought it would be useful in planning future purchases because it would allow them to consolidate purchases and possibly award more requirements contracts.

Plans to improve information

Recognizing the need for better information, CHA plans to redesign its computerized information system by 1981. Although

the new system is primarily intended to benefit the engineering and management departments through the use of a project-based cost-accounting system, it will provide some information needed to manage procurement of goods and services.

According to CHA's Controller, the new system will provide name and vendor number, method of purchases, and account charged for all purchases. The Controller and the Purchasing Agent believe that this information will result in better purchasing management.

The new system, as proposed, will provide some control over project spending versus what was budgeted. The information should also provide data which, if analyzed, would alert officials to split purchases and abuses of charge account and confirming order purchases.

According to CHA's Purchasing Agent, the ideal system would include a computerized inventory information system. This would enable CHA to monitor use of inventory items and plan future purchases. However, when such a system was recommended by a 1975 HUD study, CHA believed the cost of computerizing its inventory would be prohibitive.

#### CHA's proposed actions

We discussed our findings with CHA's Executive Director and his staff. According to the Executive Director, many of the problems we found are due to the managers' failure to adequately plan. He further stated that management controls will be tightened. Specific actions he intended to take include

--restricting the use of charge accounts, and

--requiring department director approval of all confirming purchase orders.

He also said he had ended the use of open purchase orders and assured us that the detailed budget material listings will be used to consolidate purchases and award more requirements contracts.

#### LACK OF HUD ATTENTION

HUD has not fulfilled its review responsibilities toward CHA. Until recently, HUD required a comprehensive review to identify serious management problems at all local housing authorities at least every 6 years. Current requirements call

for a review every 3 years. The timing of these reviews is to be based on HUD's knowledge of conditions at housing authorities.

HUD had not completed a comprehensive management review of CHA since 1962. In 1975 HUD responded to a series of critical newspaper articles by reviewing CHA's procurement and contracting practices and rating the operations as poor. HUD's report recommended that CHA establish a central warehouse and computerize inventory control. CHA rejected these recommendations but adopted others for changes in CHA policies and procedures concerning bid rejection and technical contracts. HUD recently began a management review which should be completed in 1982.

### CONCLUSIONS

CHA management and control of procurement activities needs to be strengthened. Controls are being circumvented by CHA staff, resulting in less than free and open competition and incomplete reporting to the Board of Commissioners. Purchases are split and open purchase orders are used to avoid formal contracting and internal reporting requirements. Small-purchase procedures, convenient but potentially costly, are abused.

CHA management lacks the necessary information to effectively manage procurement and detect these abuses. Total purchases of goods and services can only be estimated. CHA does not know where and how it is spending its purchasing dollars and thus cannot adequately plan its purchases. Recognizing its need for information, CHA is developing a new computerized information system.

HUD, which provides the majority of CHA operating income, has kept CHA solvent. However, HUD has provided little help beyond operating subsidy advances. In violation of its own requirements, HUD has not given CHA sufficient management review.

Now, when CHA is facing imminent insolvency, HUD is requesting a supplemental appropriation to clear the deficit accrued as of December 1979. Thus, the Performance Funding System, which was intended to encourage efficiency and avoid fully funding operating deficits, may be circumvented and the incentive for efficiently managing operating activities, including procurement, may be weakened.

The need for increased HUD oversight is essential to assure that housing authorities, such as CHA, are being managed as effectively and economically as possible.



RECOMMENDATIONS

We recommend that the Secretary, HUD:

- Verify as part of the current management review of CHA that actions have been taken to correct the deficiencies discussed in this report.
- Require audits and regular monitoring of financially distressed housing authorities as a prerequisite for those authorities to receive any payments in excess of those allowed under the Performance Funding System.

We discussed the report with HUD's Director of Public Housing and his staff. The Director agreed with our conclusions and recommendations. The Director said that the \$52.6 million supplemental appropriation for fiscal year 1980 does include about \$21 million to restore the CHA accrued deficit in operating reserves which existed as of December 1979. He said that every attempt possible would be made to obtain improvements in operations, including purchasing, from CHA in exchange for the supplemental appropriation.

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The information in this report is based on discussions with CHA officials, review of CHA's procurement policies and procedures, and review and analysis of data provided at CHA headquarters. We also tested CHA's procurement practices using a check list we developed for evaluating local government procurement systems. 1/ Because this was a survey, we did not verify the data provided, attempt wholesale reconstruction of data which CHA did not maintain, or specifically look for fraudulent activities. Because needed data was not available, we could not estimate the savings that could have accrued had CHA followed basic procurement principles.

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1/"Checklist and Guidelines for Evaluating Local Procurement Systems--Opportunity for Improvement in Local Government Purchasing" (PSAD-78-95, Aug. 1978).

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 3 days from its issue date. At that time we will send copies to the Secretary of Housing and Urban Development and the Director, Office of Management and Budget, and make copies available to other interested parties.

Sincerely yours,

A handwritten signature in cursive script that reads "Henry Eschwege". The signature is written in dark ink and is positioned above the typed name and title.

Henry Eschwege  
Director