

**SEMINOLE COUNTY
DEPARTMENT OF COMMUNITY SERVICES
COMMUNITY ASSISTANCE DIVISION**

**LIMITED REVIEW OF THE
NEIGHBORHOOD STABILIZATION PROGRAM**

REPORT NO. 060310

JUNE 2010

Prepared by:
The Office of the
Clerk of the Circuit Court



MARYANNE MORSE
Clerk of the Circuit Court
Seminole County

June 3, 2010

The Honorable Bob Dallari
Chairman
The Board of County Commissioners
Seminole County, Florida
1101 East First Street
Sanford, FL 32771

Dear Mr. Chairman:

I am very pleased to present you with the attached limited review of the *Neighborhood Stabilization Program*.

The review found conditions that warrant management's attention. These conditions and management's corrective action plans are included in the report that follows.

I would like to personally thank the Community Services Department personnel for their assistance throughout the course of this review. Their assistance was deeply appreciated. With warmest personal regards, I am

Most cordially,

Maryanne Morse
Clerk of the Circuit Court
Seminole County

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**Seminole County
Department of Community Services
Community Assistance Division**

**Limited Review of the
Neighborhood Stabilization Program**

EXECUTIVE SUMMARY

This report presents the results of our limited review of the *Neighborhood Stabilization Program* (NSP) grant agreement between Seminole County, Community Services Department-Community Assistance Division (the "County") and the U.S. Department of Housing and Urban Development (HUD). Our objective was to evaluate whether the County has established adequate controls over the NSP.

We concluded that:

- Inspection of rehabilitation work should be performed before approving payment to developers, audit evidence of such approval should be noted of inspections conducted;
- Work write-up or estimates submitted by developers should be evaluated for reasonableness. The work write up should be signed as evidence of review indicating proper due diligence has been exercised;
- Sub-contractors used by developers should be approved by the County as required in the developers' contracts;
- Restrictive Use Covenant should be recorded timely;
- Internal process to conduct quality control of NSP files should be developed and contract compliance should be monitored;
- Formal NSP policies and procedures should be adopted.
- No formal process exists to ensure developers' pay property taxes and insurance on NSP properties.

We have included specific recommendations following each of our findings in the Findings and Recommendations Section of this report.

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PURPOSE and SCOPE

The purpose of this limited review was to evaluate the adequacy of internal controls over nine (9) vouchers submitted for payment of rehabilitation costs, developer fees and resale of a property. The vouchers presented covered the period of October 2009 through December 2009.

METHODOLOGY

To accomplish our objectives, we:

- Interviewed Community Services Department personnel
- Reviewed:
 - Agreements with developers;
 - Work estimates and work orders for rehabilitation work;
 - Independent appraisals of properties acquired by the County on behalf of developers;
 - Lease agreements for rental properties;
 - Vouchers submitted by developers;
 - Recording of Restrictive Use Covenants;
 - Final inspections of rehabilitation work performed;

BACKGROUND

The *Neighborhood Stabilization Program (NSP)* was created under the *Housing and Economic Recovery Act of 2008*. It was established for the purpose of stabilizing communities that have suffered from rising residential foreclosures and property abandonment. The NSP permits States and local governments to purchase foreclosed homes at a discount and rehabilitate or redevelop them in order to respond to rising foreclosures and falling home values.

In November 2008, the County submitted the 2008-2009 substantial amendment One-Year Action Plan for the Neighborhood Stabilization Program (the "Plan"). In the Plan the County identified the geographic areas of greatest need based on the number of home foreclosures between August 1, 2007 and September 2008.

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BACKGROUND

Due to the number of foreclosures in the County, HUD deemed the County to be an entitlement county, which allowed the County to contract directly with HUD for the NSP funding. The NSP funds allocated to the County was based on the percentage of home foreclosures; the percentage of home financed by sub-prime mortgages and the percentage of homes in default or delinquent. The amount allocated to the County was **\$7,019,514**. The County has eighteen (18) months (June 30, 2010) to spend or obligate the funds; however, the program's end date is December 31, 2013.

In March 2009 the County sought Request for Proposals (RFP) from entities that were interested in acquiring abandoned or foreclosed properties for resale or rental to low, moderate and middle income qualified households. Qualified organizations would be required to provide the following activities:

- ***Acquire, Rehabilitate and Resale the property to income qualified individuals***
- ***Acquire, Rehabilitation and Rent the property to income qualified individuals***

Several entities responded to the RFP. Four developers were awarded contracts in July 2009. The four companies were:

1. Clarkson Concepts, Inc. – **Re-sales and Rental**
2. Miller Construction Services, LLC – **Re-sales and Rental**
3. Ruby Builders, Inc. – **Re-sales**
4. Woodard Construction Co. – **Re-sales**

The County retained an appraisal company to determine the market value of the properties. The County acquires the property discounted from the appraised value on behalf of the developer. In addition to acquiring the property, the County pays the rehabilitation costs and a developer's fee for that property. The maximum amount the County pays in rehabilitation cost is \$15,000. If the repairs needed are greater than \$15,000 the amount, subject to prior written County approval, will be increased to \$20,000.

The developer fees are listed below:

- **Re-sales** – the Developer is paid a fee of \$11,536.83¹
- **Rentals** – the Developer is paid a fee of \$9,564.33²

¹ *To date one property has been resold*

² *The Developer is also paid the discounted monthly rental income to cover the operating expenses of the unit*

BACKGROUND

Since the property is acquired in the Developer's name a restrictive use covenant is required to be recorded restricting use of the property to provide housing for low, moderate or middle income households for a period of twenty (20) years from the recording date.

In an effort to assess the established controls over the NSP, the Clerk's Internal Audit Department performed a limited review of the process in place for the Community Services Department (the Department) to ensure NSP funds are spent pursuant to the terms of the Plan submitted to HUD as well as the executed agreement with the developers.

The following were observed based on discussions with Department staff.

- *Approximately \$1.5 million of the NSP funds will be used to provide **soft second mortgages** to low, moderate and middle income qualified families.*
- *Approximately \$1.8 million will be used to acquire, rehabilitate and **provide rental** to low, moderate and middle income qualified families.*
- *Approximately \$3 million will be used to acquire, rehabilitate and **resale homes** to low, moderate and middle income qualified families.*
- *Approximately \$702,000 will be used to cover administrative expenses.*

The initial families considered in the NSP were families on the SHIP (State Housing Initiative Program) waiting list. To date the County has acquired 33 properties; 11 properties for re-sales and 22 for rental.

Internal Audit selected nine (9) vouchers for testing; four (4) were payments made to developers for rehabilitation work performed; four (4) were developer fees paid and one (1) resale of a property sold.

The four (4) developer fees tested were for rentals and were adequately supported with the executed lease agreements which entitled the developers to such fees.

As of December 31, 2009, the County has had one (1) resale. Internal Audit observed the property was resold for an amount in excess of the initial acquisition cost and rehabilitation subsidy as required in the resale contract. The net amount was disbursed to the County at the time of closing and was properly supported by the HUD-1 settlement statement.

FINDINGS and RECOMMENDATIONS

FINDING NO. 1

Inspection of rehabilitation work should be performed before approving payment to developers.

During our testing of the rehabilitation work vouchers, we observed the four (4) vouchers tested were lacking audit evidence in the files that the work performed by the developer was inspected or verified by County personnel as required in the developer agreement, sections 5(b) of the rental agreement and 5(c) of the resale agreement. Verification of the rehabilitation work being performed before payment is made is required to conform with contract requirements.

Recommendation

We recommend inspection of rehabilitation work performed by developers be conducted prior to approving payment for rehabilitation work, audit evidence of such inspection should be noted in the file and retained.

Management Response

Inspection of rehabilitation work was conducted on all units by a Community Development Project Manager; however, evidence supporting if the work was completed satisfactory or not was lacking. A memo was developed on January 7, 2010 and faxed to Internal Audit to show that a final inspection on units were inspected and completed satisfactorily.

FINDINGS and RECOMMENDATIONS

FINDING NO. 2

Work write-up or estimates submitted by developers should be evaluated for reasonableness.

We noted in most instances one developer submitted work write up/estimates for the maximum amount of \$15,000. The repair cost per square footage varied significantly from one property to the next, without consistency or basis for how County personnel evaluated the reasonableness of such estimates. Evaluating the reasonableness of the work write up/estimate submitted by the developer will raise awareness and set the tone with developers that ambiguous items will require further clarification/explanation. Moreover, evidence of review will give the assurance that proper due diligence has been exercised in considering the estimates.

Recommendation

We recommend the project managers assessing reasonableness of the work write-up sign-off as evidence of review indicating proper due diligence has been exercised in assessing the reasonableness of those costs. Items requiring further clarification or explanations from the developer should be noted in the file.

Management Response

Project Managers are responsible for reviewing work write-ups to ensure reasonable cost of the work to be performed by the developer. Amounts may vary depending on the state of the residential property; to include, but not limited to square footage, age, condition and special requirements or needs of the end buyer.

FINDINGS and RECOMMENDATIONS

FINDING NO. 3

Sub-contractors used by developers should be approved by the County as required in developers' contracts.

While testing the sample vouchers for rehabilitation work performed, we noted instances where subcontractors were used that were not approved by the County as required by Sections 3(a) of the rental agreement and 6(b) of the resale agreement. Ensuring that contract provisions are adhered to will ensure compliance with the developers' agreements and set the tone with developers.

Recommendation

We recommend the Department ensures all sub-contractors used by the developers have been approved by the County as required in Sections 3(a) of the rental agreement and 6(b) of the resale agreement.

Management Response

Project Managers will ensure subcontractors used by the developers are approved by the County as required by Sections 3(a) of the rental agreement and 6(b) of the resale agreement.

FINDINGS and RECOMMENDATIONS

FINDING NO. 4

Restrictive Use Covenant should be recorded timely.

Pursuant to Sections 3(f) of the resale agreement and 3(e) of the rental agreement “contemporaneously with the acquisition of each Property, the Developer shall also execute and record a Restrictive Use Covenant.” We observed of the nine (9) properties tested; only two (2) restrictive use covenants were recorded. Timely recording of the restrictive use covenants will ensure compliance with the contract.

Recommendation

We recommend the Department adopts procedures to ensure timely recording of the Restrictive Use Covenant as required by Sections 3(f) of the resale agreement and 3(e) of the rental agreement.

Management Response

The NSP policy has been updated to ensure that the Restrictive Use Covenants are requested in a timely manner.

FINDINGS and RECOMMENDATIONS

FINDING NO. 5

Internal process to conduct quality control of NSP files should be developed and contract compliance should be monitored.

We observed during our limited review currently a process does not exist to ensure all required documentation for a transaction/property is retained in the file. We also noted the Department personnel were not well versed with the significant contract terms and conditions of developers' resale and rental agreements.

Recommendation

Since our review was limited to merely nine (9) vouchers, we suggest the Department develops a process to ensure the NSP files contain all required supporting documentation in the event the grantor agency or any other agencies perform an operational or monitoring audit, the County would be found compliant.

Furthermore, the Department should be cognizant of the significant contract terms and conditions and establish procedures to monitor and ensure compliance with such terms and conditions.

Management Response

The Community Assistance Division Manager developed NSP monitoring checklist tools to ensure the files contain all required supporting documentation in the event internal or external operational or desk audits are performed. This will also ensure Community Development staff's due diligence with spending federal funds, to the County, end buyer, developers and other involved parties.

The compliance review will include the Program manager and the Division Manager with sample reviewing by the Department Director.

FINDINGS and RECOMMENDATIONS

FINDING NO. 6

Formal NSP policies and procedures should be adopted.

As of the report date, no formal written NSP policies and procedures have been provided to Internal Audit by the Department. During our meeting with the Department's personnel, we requested copies of the policies and procedures in place for the NSP. We were informed by the Department's HUD Administrator that the current policies are in draft form and cannot be distributed. This is not prudent business practice since the NSP has been implemented and funds have been disbursed. The policies should have been formalized and adopted prior to any distribution of funds so all personnel would be cognizant of the procedures.

Recommendation

We recommend finalizing the draft policies and procedures and adopt them so all personnel involved with the NSP will be aware of those policies and procedures. In addition, the Department should consider conducting in-house training with personnel to ensure all parties are fully aware of the required documentation from developers and should create and adapt a "checklist" for use by all staff and the checklist should be signed and placed in the file.

Management Response

The Community Development NSP policy and procedures were in draft form during the fieldwork of the limited review. This policy and its procedures continue to be updated as best practices are identified and implemented by other jurisdictions and HUD and as federal regulations from HUD are implemented; and as Community Development staff deems necessary. These newly revised procedures have been adopted by the Division Manager and Department Director.

The Division Manager will conduct a review of this policy and its procedures with all project management staff.

FINDINGS and RECOMMENDATIONS

FINDING NO. 7

No formal process exists to ensure developers' pay property taxes and insurance on NSP properties.

During our limited review we observed the Department does not have a formal process in place to monitor and ensure the developers' pay property taxes and insurance on the properties acquired with NSP funds.

We selected seven (7) properties and requested proof of property insurance or the respective declaration page of the hazard insurance policies. All of the properties selected did not contain proof of insurance in the files. The insurance policies were requested from the developers. All seven (7) properties selected had policies dated subsequent to the settlement date or the date the properties were acquired by the County. Property insurance policies for two (2) of the seven (7) properties became effective in January 2010, after Internal Audit requested such policies. It appears the insurance policies are not being obtained from the developers at the time of closing.

Recommendation

We recommend the Department implement procedures to ensure property insurance is obtained from the developers at the time of closing and property taxes are paid timely for properties acquired with NSP funds. Further, the Department should have a systematic way of monitoring the developers' so that in the event property taxes and insurance policies are not remitted timely the County would be aware of it in a timely manner.

Management Response

Project Managers are required to request a copy of insurance and taxes on residential properties at the time the developer is given approval to proceed with acquisition. A copy of the taxes and insurance will be submitted to the Housing Customer Service Specialist for data entry and filing. The Housing Customer Service Specialists monitors payment of property insurance and taxes on an annual basis to ensure all properties are insured and taxes paid.