



## **MANAGEMENT ACTION PLAN PROGRESS REPORT**

DATE: March 16, 2018

TO: Jim Gray, Mayor

CC: Sally Hamilton, Chief Administrative Officer  
Glenn Brown, Deputy Chief Administrative Officer  
Aldona Valicenti, Chief Information Officer  
Janet Graham, Commissioner of Law  
Charlie Lanter, Director of Grants and Special Programs  
Phyllis Cooper, Director of Accounting  
Susan Straub, Communications Director  
Urban County Council Members  
Internal Audit Board Members

FROM: Bruce Sahli, CIA, CFE, Director of Internal Audit

RE: Grants Housing Rehabilitation Program Audit MAPPR

### **Background**

On January 24, 2017 the Office of Internal Audit issued the Grants Housing Rehabilitation Program Audit Report. The 2017 audit report contained several findings related to moving the inspection process to the Division of Code Enforcement, the incorrect handling of a mortgage payoff, inappropriate or inconsistent rehabilitation activity, the need to update the Rehab Program Policy, the need for improved access to the program's financial information, issues with the handling of mortgages and loans, inconsistent application of inspector standards, and issues with projects exceeding bid amounts.



This review is provided for management information only. It is not an audit and no opinion is given regarding controls or procedures. The period of review included Rehab Housing projects from July 1, 2017 through February 28, 2018.

The original audit report issued on January 24, 2017 contained the responses of the former Director of Grants & Special Programs, who retired effective February 1, 2017. A subsequent response was received on June 26, 2017 from the current Director which supersedes the former Director's responses. This Management Action Plan Progress Report examined the current Director's action plans to determine if the findings have been addressed.

A summary of the findings from the original audit report and a summary of the results of our follow-up are provided in the table below. The original findings, current management's responses, and details of the results of this follow-up are contained in the **ORIGINAL AUDIT RESULTS AND FOLLOW-UP DETAILS** section of this report.

Finding	Summary of Original Finding	Follow-Up Results
Finding 1 High Priority	Grants Inspection Process Should be Moved to the Division of Code Enforcement	This function has not been moved to Code Enforcement. Based on the action plans put in place to address the other findings, and the Director's research of the recommendation and logic for keeping this function in the Divisions of Grants & Special Programs, the decision to retain this function is deemed reasonable. The finding is resolved.
Finding 2 High Priority	Incorrect Handling of a Mortgage Payoff	Language has been added to the Rehab Policies & Procedures that addresses the situation identified in the original finding. Division of Grants & Special Programs management indicated this situation has not occurred again. Should it occur again, it will be addressed going forward with a clearly defined procedure. The finding is resolved.



<p><b>Finding 3</b>  <b>High</b>  <b>Priority</b></p>	<p><b>Inappropriate or</b>  <b>Inconsistent</b>  <b>Rehabilitation Activity</b></p>	<p>The Housing Rehab Program Policies &amp; Procedures have been updated to improve the control of change orders. Change orders tested included detailed explanations and the Grants Director's signature indicating his review and approval. Project files reviewed contained detailed write-ups of work required and photos as needed. The Grants Compliance Supervisor performed an on-site review of those rehab projects after the initial inspection was completed. The finding is resolved.</p>
<p><b>Finding 4</b>  <b>High</b>  <b>Priority</b></p>	<p><b>Rehabilitation Program</b>  <b>Policy Needs to be</b>  <b>Clarified and Updated</b></p>	<p>The Rehab Program Policies &amp; Procedures have been updated and clarified. The maximum rehab limit has been increased to \$35,000. A Tier system is in place to allow the most severe issues and code infractions to be addressed even if full rehabilitation cannot be achieved within the maximum rehab limit. The finding is resolved.</p>
<p><b>Finding 5</b>  <b>High</b>  <b>Priority</b></p>	<p><b>Grants Manager Lacks</b>  <b>Access to Financial</b>  <b>Information</b></p>	<p>RehabPro software currently cannot perform financial tracking, so this is being performed on an Excel spreadsheet. The Director stated that the financial tracking has improved the management of funds. Management produces a Monthly Finance Report that tracks available funds by CDBG or HOME grant, which serves as the agenda for the monthly finance and budget meetings for the Rehab Program. The finding is resolved.</p>



<p><b>Finding 6</b> <b>High</b> <b>Priority</b></p>	<p><b>Issues Noted with Mortgages and Loans That Could Affect LFUCG's Collateral Position</b></p>	<p>Updated language regarding POA's is included in the revised Policies &amp; Procedures. The Grants Manager stated this process is being followed, and our detail testing verified compliance with the updated Policy. Adherence to the revised processes regarding closed loans and the release of matured loans was verified in meetings with the Grants Director and Grants Manager. The finding is resolved.</p>
<p><b>Finding 7</b> <b>High</b> <b>Priority</b></p>	<p><b>Inconsistent Application of Inspector Job Standards</b></p>	<p>A tracking sheet of current Grants Compliance Officer licenses and their expiration dates is being maintained by the Grants Compliance Supervisor. All licenses are up to date. The finding is resolved.</p>
<p><b>Finding 8</b> <b>High</b> <b>Priority</b></p>	<p><b>Projects Examined Consistently Exceeded Bid Amounts</b></p>	<p>The revised Rehab Program Policies &amp; Procedures require the approval of all change orders by the Director of Grants &amp; Special Programs, and that each change order must clearly indicate the reason for the change. Our sample of change orders verified that Policy is being adhered to. The Director also stated that change orders are discussed in weekly meetings and there have been no change order problems with contractors. The maximum project amount has been increased to \$35,000. The finding is resolved.</p>



## SUMMARY OF AUDIT FINDINGS

### **Original Finding #1: Grants Inspection Process Should be Moved to the Division of Code Enforcement**

**Priority Rating: High**

#### **Condition:**

The Division of Grants & Special Programs currently employs two Code Enforcement Officers and one Code Enforcement Supervisor to provide inspections for its Housing Rehab Program. The audit identified findings of Inappropriate or Inconsistent Rehabilitation Activity (Finding #3), Rehabilitation Program Policy Needs to be Clarified and Updated (Finding #4), Inconsistent Application of Inspector Job Standards (Finding #7), and Projects Examined Consistently Exceeded Bid Amounts (Finding #8).

#### **Effect:**

Code Enforcement inspections under the management of a Division lacking the expertise to manage this function could result in inefficient and ineffective inspections. It could also result in financial decisions taking precedent over inspection results.

#### **Recommendation:**

The Housing Rehabilitation Program inspection process should be moved to the Division of Code Enforcement. The Division of Code Enforcement performs similar work and has the organizational structure to support the duties of such work with management and staff well trained in Code Enforcement. Moving the Grants inspection function to Code Enforcement would ensure it is managed by LFUCG personnel with a clear understanding of Code Enforcement processes, procedures, and practices to provide consistent quality in the inspection process. This move would also separate the financial approval and housing inspection functions of the Housing Rehab Program, and would reduce any potential influence those two functions may have over each other.

#### **Director of Grants and Special Programs Response:**

Since starting as the Director of Grants & Special Programs on March 20, 2017, I have met with the division's Code Enforcement Officers and separately with the Division of Code Enforcement in response to this finding in order to explore the recommendation and its implications. Additionally, I spoke with staff members operating comparable housing rehab programs in other communities and found that in no case were the inspectors performing this work operationally housed within that city's equivalent Division of Code Enforcement. It seems this move would be highly unusual among



community development programs, likely due to the expertise required to perform other, unrelated functions in the division as well as the need for arm's length separation between the staff members who cite homes for code violations and the staff members who help homeowners repair those violations.

This recommendation is derived from other findings in the report (#s 3, 4, 7, and 8) and states that having inspections within a division “lacking the expertise to manage this function could result in inefficient and ineffective inspections.” While I don’t dispute that conclusion, those results can be easily avoided through clear and consistent policies and procedures and proper training and communications. We believe that such guidance and communication now exist as described below in response to other findings. Therefore, it is not my intention to move the inspection process to the Division of Code Enforcement at this time.

However, it seems necessary to further clarify the role of the inspectors and differentiate their work inspecting homes for rehab purposes and performing other HUD-required monitoring and compliance inspections from the work performed in the Division of Code Enforcement. Therefore, I recommend retaining the job description and class but changing the functional title of the inspectors from Code Enforcement Officer to Grants Compliance Officer. This functional title better reflects the work performed by these employees and reduces confusion of roles with the Division of Code Enforcement. In fact, the Director of the Division of Code Enforcement told me he also would have recommended this change should the employees have been relocated to his division.

Finally, I have taken steps to ensure improved communication internally and externally with the implementation of regular staff meetings in which the Code Enforcement Officers may discuss concerns and specific needs and projects. I have also streamlined communication between the Division of Grants & Special Programs by agreeing, with the Director of Code Enforcement, that only supervisors in his division will work with designated staff members in Grants to share information regarding applications and pending home rehab jobs. This eliminates a significant amount of informal, ad hoc communication involving multiple Code Enforcement Officers from both divisions.

#### **Follow-Up Detail Results:**

**This function has not been moved to Code Enforcement. Based on the action plans put in place to address the other findings, and the explanations provided by the Director regarding his research of the recommendation and his logic for keeping this function in the Divisions of Grants, the decision to retain this function is deemed reasonable. The finding is resolved.**



**Original Finding #2: Incorrect Handling of a Mortgage Payoff**  
**Priority Rating: High**

**Condition:**

During the audit we examined the circumstances surrounding a Rehab project that was later destroyed by a fire. An insurance check was written from the homeowner's insurance company to the primary lienholder (Seterus), secondary lienholder LFUCG, and the homeowner Mr. Woodrum (all listed on two insurance checks as co-payees). A series of e-mails between the Department of Law and the Grants Manager ensued.

On December 14, 2015 the Grants Manager wrote the following email to a Department of Law Attorney: "I have the checks (insurance company checks paying for the fire damage) in our servicing file; I did not think I should deposit them after reviewing the check endorsements as both look to be signed by Mr. Woodrum (the homeowner)." Copies of the checks were attached to this email. On December 15, 2015 the Attorney's email reply stated: "Please hold onto the checks for the time being."

On December 16, 2015 Seterus faxed the Payoff Statement to the Division of Grants & Special Programs. The Payoff Statement specifically stated that the amount owed to Seterus was \$71,319.70.

On January 4, 2016 the Grants Manager sent an email to the Department of Law Attorney stating: "We have the Payoff Statement from Seterus, Inc and the Quit Claim Deed from Vickie Lloyd Woodrum. Can't we deposit the checks, keep our payoff amount, then cut a check to Seterus, Inc, and the remainder to Mr. Woodrum?" On January 5, 2016 the Attorney's email replied: "No. Not at this time."

On January 11, 2016 the Department of Law Attorney sent the following email to the Grants Manager: "Please take the checks to Laura Harris in the Revenue Department for processing. She will process the checks and indorse them on behalf of LFUCG. After the checks have been processed, please send them priority mail express, return receipt requested to the following address:

Seterus, Inc.  
Attn: Loss Draft Services Department  
P.O. Box 52009  
Phoenix, AZ 85072-9808"



On January 11, 2016 Laura Harris (Revenue Supervisor) sent the following email to the Grants Manager: “(Grants Manager) the deposit is done.....”

On January 20, 2016 Mr. Woodrum faxed a handwritten letter to the Division of Grants & Special Programs. The letter states, “This is to inform you of my agreement with LFUCG on paying off the mortgage on 3158 Leestown Road.....After LFUCG takes there amount from these two checks they are to send a check to Seterus due in the amount of \$58,601.32.” The letter goes on to state that a check should be sent to Mr. Woodrum in the amount of \$54,353.77.

On January 20, 2016 the Grants Manager emailed the Revenue Supervisor: “Do we know if these checks cleared?” The Revenue Supervisor’s email reply was: “We haven’t received anything back from the bank so far.” The Grants Manager email reply was: “Is it too soon to do a JE and check request?” The Revenue Supervisor email reply was, “I would think its fine we should have heard by now if they were going to reject it.”

On January 21, 2016, LFUCG cut a check to Seterus in the amount of \$58,601.32 and another check to Mr. Woodrum in the amount of \$54,353.77.

**Effect:**

This produced three issues: 1) The homeowner (Mr. Woodrum) may have been paid more than he was entitled to, 2) LFUCG (the lesser lienholder) had its lien paid in full, and 3) primary lienholder Seterus’s payment was approximately \$13,000 less than the amount they stated they were owed in the Payoff Statement received by the Division of Grants & Special Programs on December 16, 2015.

The Law Department is currently addressing this issue in ongoing court proceedings related to this matter.

**Recommendation:** Payoff amounts should only be determined by an official document from the mortgage company.

**Director of Grants and Special Programs Response:**

This finding was the result of miscommunication in one very specific case. After consultation with the Department of Law, the program policies and procedures have been revised to state the following:



“If an insurance claim check issued in the name of the homeowner, a first mortgage lender and LFUCG, the Grants Manager will contact the first mortgage lender and obtain direction in writing from that entity on how to proceed. Under no circumstances should the check be endorsed or deposited by LFUCG unless directed in writing by the first mortgage lender.” (Policies & Procedures, Page 19)

The Grants Manager has been instructed to follow this policy going forward.

### **Follow-up Detail Results:**

**The additional language to the Rehab Policies & Procedures has been verified. Discussions with the Director of Grants & Special Programs and the Grants Manager determined that this policy is being followed, and there has not been another incident like the one in the original finding. This was an unusual situation identified by the prior audit, and should it occur again it will be addressed going forward with a clearly defined procedure. The finding is resolved.**

### **Original Finding #3: Inappropriate or Inconsistent Rehabilitation Activity** **Priority Rating: High**

#### **Condition:**

We identified numerous instances of inconsistent adherence to the Division of Grants & Special Programs Rehab Policies, as noted below.

#### Approved Rehab Project Findings:

- Two homes had LFUCG liens totaling \$5,745, which according to Grants Rehab Policy should have disqualified the homes. Grants Rehab Policy states that “Applications will be denied for those homeowners who have delinquencies with LFUCG, or state or federal liens”. One of the properties also had outstanding property tax liens and federal tax liens. (This is referred to as Case #1 in the Director’s Response.)
- One homeowner had a lien on her property due to an old medical debt which is now set up on a payment plan. This information was not included in her application, which is relevant to her debt to income ratios and the percentage of income going to service debt payments. (This is referred to as Case #2 in the Director’s Response.)



- One home had sewage in the crawlspace, which per Grants management is an automatic disqualifier. However, Grants paid to have the sewage pumped out and fans were installed to dry the ground. Lime, soil, and gravel were also later laid over the entire crawlspace. We noted that other homes were denied due to sewage being in the crawlspace. Inconsistency in approving Rehab Program funds could lead to claims of discrimination or favoritism. (This is referred to as Case #3 in the Director's Response.)
- One home had an initial Grants Rehab inspection estimate of \$26,339, while in another instance the homeowner accepted a bid of \$25,950. Both exceeded the \$25,000 limit set by Grants Rehab Program Policies. Many other homeowners were denied Rehab funds due to their estimate exceeding \$25,000. (This is referred to as Case #3 and #4 in the Director's Response.)
- One rehabilitated home had brackets installed for curtains through a change order that used additional funds. If curtains were in the house before the rehab, they should have been re-installed and not replaced. If these were new curtains, their installation would be purely aesthetic and should not have been installed. In either instance, this was an inappropriate additional charge, and documentation regarding this installation was insufficient to determine if these were new or existing curtains. (This is referred to as Case #5 in the Director's Response.)
- One home's loan was closed in 2012, but work continued to be completed with Grants Rehab Program funds through at least August 2014. Per the Loan Agreement, the original contractor had a warranty on all work completed and should have been responsible for completing the additional work, while the relationship between LFUCG and the homeowner should have ceased when the project was closed. (This is referred to as Case #6 in the Director's Response.)
- A homeowner complained after their rehab was completed that the contractor refused to honor the rehab warranty he gave the homeowner. Grants paid for the complaints to be settled, which was inappropriate since a valid warranty was in place, and per the Loan Agreement this should have been an issue between the homeowner and the contractor. It is an inconsistent application of the Rehab Program to pay for the settlement of rehab complaints for one homeowner if that option is not available to all Rehab Program homeowners. (This is referred to as Case #5 in the Director's Response.)
- Pictures and documentation in one home's file indicated that decorative stone was added to a wall in the kitchen for no specified reason. While this addition was not requested by Grants, Grants did pay for the decorative stone wall. Funds should not have been paid for decorative stonework, and if the contractor still chose to



install it then the cost should have been the contractor's and/or homeowner's financial responsibility. (This is referred to as Case #5 in the Director's Response.)

- One rehabilitated home had a change order issued for \$56,224 which brings into question the thoroughness of the original inspection and estimate. After the loan was closed, an external contractor from a Structural Consulting Engineer firm suggested this house should be demolished rather than being rehabilitated, suggesting that this Rehab project wasn't thoroughly inspected and properly cost estimated. (This is referred to as Case #5 in the Director's Response.)
- One homeowner resided at Candlewood Suites for 246 nights at a cost of \$14,447 while her home was being rehabilitated. This house had a lead based paint issue that required abatement, which qualified the homeowner to have temporary relocation with a cost not to exceed \$3,000. (Per Grants Rehab Policy, in situations where the homeowner cannot relocate on their own, temporary relocation benefits are available at a maximum limit of \$3,000). The Policy states that the amount may be increased with prior written approval from the Division Director if certain criteria are met. The Policy also states that any relocation expenses exceeding \$3,000 must be paid by the homeowner unless the contractor is charged liquidated damages, which did not occur in this situation. The cost of the entire 246 nights was paid by Grants. The Director noted that "Homeowner could not have paid the excess relocation costs. We also were not in a position to charge liquidated charges to the contractor, given that the problem was of our creation." It therefore appears that this excessive relocation cost was due to some issues regarding the inspection process. The Rehab Policy is therefore inconsistently written regarding the maximum allowable relocation expense, which may have contributed to the approval of such an expensive relocation cost. (This is referred to as Case #5 in the Director's Response.)
- In one Rehab project, the Division of Grants & Special Programs Code Enforcement Officer personally sold items for the homeowner, a service which was not part of the contract. The homeowner was subsequently forced to make several attempts to contact the Code Enforcement Officer regarding these sold items to receive payment. Grants Management was aware of this situation per the loan file, but no documentation of a resolution was found. The same situation recently occurred on another Rehab project. Per the Director of Grants and Special Programs, a statement prohibiting this sort of activity has since been added to their Rehab Policy. (This is referred to as Case #5 in the Director's Response.)
- One Rehab home had the ceilings painted, although apparently no work was done to the walls. It's possible this could have been warranted if the ceiling paint was heavily deteriorated, or it could have been done purely for aesthetics which is not



allowed. The reason for this ceiling work was not documented. (This is referred to as Case #6 in the Director's Response.)

- One Rehab project's file included a memo from the Code Enforcement Supervisor noting that the property was infeasible due to a crawlspace being too low. The homeowner subsequently completed some work themselves on the home, none of which would have altered the crawlspace. The home was then approved for Rehab. This is an inconsistent application of Grants Rehab policy, as many homes are denied due to low/unsafe crawlspaces. (This is referred to as Case #6 in the Director's Response.)
- One home had the basement waterproofed which is not allowed per Grants Rehab Policy. Grants Policy states, "Work in basements finished or not will be limited to structural repairs and mechanical repairs and equipment. Abatement of water intrusion into basement or crawl space will be limited to proper management of surface water and or sump pump installation." This was another example of inconsistent application of Policy, adding to the inspectors' confusion regarding what is and is not allowable rehab work. (This is referred to as Case #7 in the Director's Response.)

#### Denied Rehab Project Findings:

- Two homeowners applied for rehab and were not denied until approximately one year later. The disqualifying issues should have been noted immediately. In one instance, the homeowner applied in July 2015 and was put on the waitlist, but was not denied until May 2016 due to the property not being registered in her name. In the other instance, the homeowner applied in August 2014 and was not denied until December 2015. The disqualifying factor was that she wasn't yet eligible for a second rehab of her home. Per the Grants Manager, this information was readily available and it is standard practice to check these items prior to placing a homeowner on the waitlist.
- Grants paid for title work and an appraisal in July for one homeowner, yet did not complete the financial analysis until October. When the homeowner was denied for financial reasons other than title/appraisal problems, the costs of these two services had already been incurred.

#### Effect:

The lack of consistent application of Grants Rehab Policies and Loan Agreements could lead to claims of discrimination or favoritism by other applicants. It can also contribute to unnecessary costs being incurred.



**Recommendation:**

Each home considered for rehab should have a thorough and adequate inspection process, and all findings (whether noted by the Code Enforcement Officers or later by the contractor in a change order) should be properly vetted in a manner consistent with the other homes considered in the Program. Change orders should have thorough descriptions explaining the need for the additional funds and should be reviewed carefully to ensure it is appropriate and meets the Program's standards. Inspection documentation from the Code Enforcement Officers should include detailed write-ups and photos to assist with analysis and decision making. Before, during, and after project completion photographs should be placed in each Rehab project file. The application process should be changed to allow the financial analysis to be completed prior to paying for outside services to ensure the financial requirements are met prior to the start of any Rehab project.

**Director of Grants and Special Programs Response:**

The Housing Rehab Program Policies & Procedures have been rewritten with significant programmatic changes to take effect on July 1, 2017. The newly updated program requirements provide clarity and direction regarding the application and inspection process all the way through to closing and, if followed, ensure consistency. Change orders are now required to include thorough descriptions explaining the need for additional funds and must be reviewed and signed by the Division Director in addition to the Code Enforcement Supervisor (Policies & Procedures, Page 32). Inspectors have been instructed to include detailed write-ups and photos for analysis and decision making and to properly include those in the RehabPro software. The Code Enforcement Supervisor has been charged with ensuring consistency across those inspections and compliance with the required details for inspection write ups.

In addition, the newly revised policies and procedures require the financial analysis to be completed prior to any outside services that incur cost except for those required for the financial analysis, such as credit reports or title searches. This addresses the concern of expending resources on homes which are later deemed infeasible or otherwise ineligible for assistance.

**Follow-Up Detail Results:**

**A review of the Housing Rehab Program Policies & Procedures noted that, "All change orders must be approved by the Division Director and indicate the reason for the request, including whether an item should have been identified upon inspection; was the result of unavoidable circumstances; was contractor error in**



bidding; or other possible causes. Under no circumstances should change order work begin without approval from the Division Director. The Grants Compliance Supervisor will track reasons for change orders so that avoidable causes may be addressed.”

Our testing of change orders occurring since July 1, 2017 confirmed they include detailed explanations of the changes orders, including if the issue was one that should have been identified during the feasibility inspection. The Grants Director had signed off on all change orders to denote his review and approval. A review of the project files noted they contained detail write-ups of work required to rehab the property, and included photos as needed. Per discussion with the Grants Compliance Supervisor and examination of project files, the Grants Compliance Supervisor is performing an on-site review of all rehab projects after the initial inspection is done by the Grants Compliance Officer. The Grants Compliance Supervisor had signed off on the project feasibility inspection forms to document his review. The documentation is considered sufficient to comply with the new inspection requirements.

The finding is resolved.

**Original Finding #4: Rehabilitation Program Policy Needs to be Clarified and Updated**

**Priority Rating: High**

**Condition:**

During the Audit, all three Code Enforcement Officers noted they did not think they had clear guidelines for the inspection process. Our review of a sample of approved and denied homes identified inconsistencies that support this position (see Finding #3). We were also informed by Grants management that the Rehab Policy currently in place is most likely the original Policy from the inception of the Program that has been altered over time. Grants management stated that Grant’s \$25,000 limit for rehabilitating homes has been in place for about 20 years, so it is likely the Rehab Policy dates back to the 1990’s. We further noted that the Rehab Policy does not provide guidance for inspectors that may find themselves in a hazardous situation while conducting an inspection. For example, a contractor informed an inspector that the homeowner was using heroin while the contractor was present in the house. Inspectors should be informed what to do if such an event occurred during an inspection.



**Effect:**

The lack of clear and consistent Policies leave Code Enforcement Officers in a position where their decisions can be incorrect or questionable, and can result in homes being incorrectly recommended for rehabilitation or incorrectly refused for rehabilitation. The \$25,000 limit does not take into account the increased cost of home repairs over the past 20 years.

**Recommendation:**

The Rehab Program Policy and the Quick-Specs should be reviewed and updated as necessary by qualified personnel to ensure that they meet the requirements for the Rehab Program. This should be done with input from the Grants Code Enforcement Officers and the Division of Code Enforcement to include their expertise in this area. The \$25,000 Rehab limit should be re-evaluated to determine if it is still a realistic standard when compared with current home reparation costs. The revised Policy should consider approving the completion of \$25,000 (or more, if the limit is increased) of the most severe issues and code infractions versus not approving the project at all. For example, a leaking roof could be fixed in addition to unsafe electrical wiring, while less pertinent issues such as painting, patching holes, replacing garage siding, etc. might not be completed as they are less severe. This would allow homeowners to obtain assistance in the most severe circumstances while still allowing Grants to ensure the funds are used in the best possible way. The Policy should also include instructions regarding an inspector's authority to vacate a home being inspected if he/she experiences an unsafe or potentially dangerous situation.

**Director of Grants and Special Programs Response:**

The Housing Rehab Program Policies & Procedures have been rewritten with significant programmatic changes to take effect on July 1, 2017. This revision included significant input from and consultation with the Grants Manager overseeing the program; Code Enforcement Supervisor and Code Enforcement Officers who perform inspections; contractors who perform work on houses; and the Division of Code Enforcement. Among the most significant changes, the maximum amount that may be spent on rehab has been increased to \$35,000. Additionally, the revised policy allows the completion of up to \$35,000 of the most severe issues and code infractions versus not approving the project at all. The revised policy includes a "Tier" system of measures which provide guidance to the staff members for prioritizing work on a home (Policies & Procedures, Page 36). The Quick-Specs are reviewed annually by the Code Enforcement Supervisor and his staff members and will continue to be updated on that timeline.



In addition, the revised policy includes instructions regarding an inspector's authority to vacate a home being inspected if he or she experiences an unsafe or potentially dangerous situation. The newly revised policy on this matter now reads:

“Note: If the house is too cluttered, is a health or safety hazard to the Code Enforcement Officer, or has important areas that are not accessible by the Code Enforcement Officer, then the inspection will not be performed and the Code Enforcement Officer will notify the owner that the conditions will have to be remedied before the house can be inspected. At no time will a Code Enforcement Officer be obligated to complete an inspection under conditions they deem unsafe.  
“ (Policies & Procedures, Page 24)

### **Follow-up Detail Results:**

We verified that all of the new language mentioned in the Director of Grants & Special Programs response has been added to the Rehab Program Policies & Procedures. The maximum rehab amount has been increased to \$35,000. A Tier system is in place that will allow the most severe issues and code infractions to be addressed, even in those situations where full rehabilitation cannot be achieved within the maximum rehab limit of \$35,000. The finding is resolved.

### **Original Finding #5: Grants Manager Lacks Access to Financial Information** **Priority Rating: High**

#### **Condition:**

We determined that the Grants Manager charged with the day to day operations of the Rehab Program is excluded from information regarding the program budget and fund balances for the related grants. As a result, inspectors could conduct 1<sup>st</sup> and 2<sup>nd</sup> inspections, she could complete the financial analysis, hire a contractor to rehab a home, and only then be told there are insufficient funds to complete the project. Rehab Pro has the ability to track this information, and Grants is paying Happy Company (the owner of Rehab Pro) for two employees to manage Rehab Program budgeting/accounting, yet neither employee utilize this feature on Rehab Pro.

#### **Effect:**

Lack of pertinent financial information prevents the Grants Manager from making the best decisions regarding how Rehab Projects are financially managed.



**Recommendation:**

The Grants Manager charged with this program should have full access to financial information, including fund balances, in order to ensure she is managing the financial aspects of the program in the most efficient manner possible.

**Director of Grants and Special Programs Response:**

Effective July 1, 2017, the total amount of funding available to the Home Rehab Program will be entered by funding source and year into the RehabPro software. This begins the fiscal year with a total from which the Grants Manager operating the program can manage program finances and know at all times the remaining funds available. This will be monitored monthly to ensure it is consistent with actual funds available in PeopleSoft. Additionally, the newly revised program policies and procedure require that the final expense totals and funds charged for each home are entered into RehabPro at the close of each individual project (Policies & Procedures, Page 10). This will ensure an accurate running balance from which the Grants Manager operating the rehab program can manage the finances.

Also, effective immediately, I have implemented monthly finance and budget meetings including the Grants Manager operating the rehab program; the Code Enforcement Supervisor; the Grants Manager (Finance & Accounting); and other appropriate staff. In this monthly meeting the staff will review spending and budget status in the home rehab program to ensure coordination and that the Grants Manager responsible for the rehab program has complete and accurate information for financial management.

Financial tracking in RehabPro will serve as an additional aide to staff but will not supersede PeopleSoft for official financial management of the program and all staff will continue to utilize PeopleSoft as a primary financial tool.

**Follow-Up Detail Results:**

**Discussions with the Director of Grants & Special Programs and members of his management team confirmed that RehabPro currently cannot perform financial tracking, so this is being performed on an Excel spreadsheet. The vendor is trying to address the tracking issue in RehabPro. The Director stated that the financial tracking has improved the management of funds.**

**The Grants Manager also produces a Monthly Finance Report that tracks available funds by CDBG or HOME grant. The Monthly Finance Report serves as the agenda for the monthly finance and budget meetings where Rehab Program spending and budget status is discussed.**



**This process is considered sufficient to account for final expense totals and funds charged.**

**The finding is resolved.**

**Original Finding #6: Issues Noted with Mortgages and Loans That Could Affect LFUCG's Collateral Position**

**Priority Rating: High**

**Condition:**

We reviewed the general practices of recording and releasing mortgages. A sample of mortgages determined that it took an average of 53 days for a mortgage to be recorded at the County Clerk's Office. Four mortgages were also found to have been released early with no explanation provided after being researched by the Grants Manager and the Administrative Specialist Principal. Two of these mortgages were released 10 years early, one 11 years early, and one eight months early.

One loan selected during testing had a loan origination date of June 16, 2016 but had not been recorded with the County Clerk's Office as of October 12, 2016 due to an improper Power of Attorney (POA). The Grants department took the word of the loan applicant that the POA was recorded with the Clerk's Office and allowed this person to sign for the loan. Grants was aware of this issue prior to the Auditor alerting them, and stated they have been working to get a new limited POA written and signed.

**Effect:**

Kentucky law states that mortgage positions are based upon first to record, so LFUCG's position as a mortgage lien holder is put at risk any time the loan is not recorded in a timely manner. Early mortgage releases harm LFUCG's lien position in the property in the event there is a refusal to pay the mortgage.

**Recommendation:**

Grants should work with the Department of Law to ensure the proper steps are taken to validate LFUCG's position on the unrecorded property. Grants noted that they have now changed their procedure to always validate that a POA is recorded prior to signing a loan. A new Policy should also be put into place stating an appropriate length of time to record a mortgage and ensure training is adequate in regards to mortgage releases. We recommend that all such mortgages be recorded within two days of being executed.



### **Director of Grants and Special Programs Response:**

The Division has made several policy and procedure changes to address this finding. Each of the bulleted items below has been added directly to the program's updated policies and procedures.

- “When applicable, Grants staff must always validate that a POA is recorded prior to signing a loan.” (Policies & Procedures, Page 10)
- “Once a loan is closed, the mortgagor has a 3-day right of rescission to cancel the loan. The outside attorney will be contacted immediately after (within the first working hour) the 3-day rescission expires to come by the office and sign the mortgage within seven working days. Grants staff will walk/drive documents to the attorney if necessary. Grants staff will record in the County Clerk's Office within one business day of signing by the attorney.” (Policies & Procedures, Page 10) NOTE: The audit recommended that mortgages be recorded within two days of being executed. This is not possible due to the 3-day right of rescission but the above policy change was developed in consultation with the Department of Law and we believe satisfies the intent of the recommendation.
- “On the 5<sup>th</sup> and 20<sup>th</sup> day of each month (or the first work day following a Saturday, Sunday, or holiday), the Grants Manager will prepare releases for loans that have matured, send them to the Department of Law and Chief Administrative Officer for signatures, and record with the Fayette County Clerk's Office by the end of the next working day. Releases that occur as a result of a pay-off will be recorded within ten days of receipt of funds. Releases that occur as a result of a foreclosure will be recorded with ten days of notice of case closed from the Department of Law. “ (Policies & Procedures, Page 22).

### **Follow-Up Detail Results:**

**We verified that the language regarding Power of Attorneys is included in the revised Policies & Procedures. Discussion with the Grants Manager confirmed this process is being followed, and our detail testing determined that a POA is obtained in a timely manner when necessary. Adherence to the revised processes regarding closed loans and the release of matured loans was verified in meetings with the Grants Director and Grants Manager. The finding is resolved.**



**Original Finding #7: Inconsistent Application of Inspector Job Standards**  
**Priority Rating: High**

**Condition:**

The LFUCG Code Enforcement Officer Job Description requires a One and Two Family Dwelling Inspector certification within the six month probation period, and that it be maintained as a condition of continued employment. As of the completion of audit fieldwork, the newest Code Enforcement Officer did not hold an inspector's license. This employee has passed their probationary period, has done numerous 1<sup>st</sup> inspections, one 2<sup>nd</sup> inspection, and is acting as a Code Enforcement Inspector in all aspects of the job. Per Grants' Administrative Policies and Procedures, only two inspectors are allowed to conduct 2<sup>nd</sup> inspections, and the newest Code Enforcement Officer is not one of them. We were also informed that other Code Enforcement Officers have been suspended or reprimanded if their licenses lapsed.

**Effect:**

Inconsistent application of the inspector's license job requirement could raise questions regarding the quality of Rehab Project inspections and allegations of management favoritism.

**Recommendation:**

The job requirement that all inspectors hold current inspector licenses should be consistently applied.

**Director of Grants and Special Programs Response:**

The job requirement that all inspectors hold current inspector licenses will be consistently applied. The Code Enforcement Supervisor is responsible for ensuring that he and each of the Code Enforcement Officers reporting to him maintains current licenses; obtains required continuing education; and follows all legal and policy requirements associated with inspections and licensing. The Code Enforcement Supervisor has been instructed that this is his responsibility.

As a backup measure, I have created a license tracking sheet (see attached) to be maintained by the Division's Administrative Specialist Senior. The Administrative Specialist Senior will be responsible for monitoring the sheet monthly and sending reminders to the Code Enforcement Supervisor and respective Code Enforcement Officers when licensure expiry is approaching. The Administrative Specialist Senior will notify the Code Enforcement Supervisor and Division Director immediately should an employee's licensure lapse and that employee – in addition to facing appropriate



disciplinary action – will not be permitted to perform relevant work until the license has been obtained. This applies to new and current Code Enforcement Officers.

NOTE: The Administrative Specialist Senior is currently on long-term leave and may not return to work. The Division Director will maintain this function until that employee returns or is replaced.

**Follow-Up Detail Results:**

A tracking sheet of current Grants Compliance Officer licenses and their expiration dates is being maintained by the Grants Compliance Supervisor. All licenses are up to date. The finding is resolved.

**Original Finding #8: Projects Examined Consistently Exceeded Bid Amounts**  
**Priority Rating: High**

**Condition:**

During our testing of a sample of 17 approved Rehab projects, we noted that 100% of these projects went over the contractor's original bid by an average of \$5,823.12 or 15.2%. One project went over by \$56,224 or 64.3%. A contingency of 10% is currently set up for project cost overruns, but does not appear to be a sufficient amount.

One contractor we examined exceeded the bid amount on all three Rehab Projects he completed by an average of 27%. This contractor was removed from the Contractor List for reasons unrelated to the cost overruns.

**Effect:**

When actual costs consistently exceed contract bids, this is an indication that the project costs are underestimated and/or that project change orders are not properly monitored and controlled.

**Recommendation:**

Grants Management should review completed projects to determine the reason(s) for project costs exceeding the original bid amount. Any trends identified by this review should be analyzed and proper action taken to limit such overruns in the future. Cost overruns could be the result of an inadequate inspection by Grants, unforeseen circumstances found during the rehab, or a contractor underbidding in order to secure



the project. We also recommend considering adjusting the contingency amount to help ensure loan amounts are more closely aligned with the true costs of a rehab.

### **Director of Grants and Special Programs Response:**

While it's true that many home rehab projects experience cost overruns for unavoidable reasons, I believe the significant number of overruns encountered during this audit will be addressed by two changes previously discussed.

First, all change orders must now be approved by the Division Director with clear indication of the reason for the change (Policies & Procedures, Page 32). Upon investigation I determined it is possible that some contractors are abusing the change order process. Contractors have been informed of this change and of the intent to reduce the number of approved change orders. The Grants Manager will track the reasons for change orders and identify trends to the Code Enforcement Supervisor and Division Director so that the issue can be addressed. If caused by inadequate inspections, for example, a Code Enforcement Officer may require additional training or even disciplinary action for poor performance. If caused by contractor underbidding, then contractor sanctions up to and including debarment from the program may be implemented.

Second, the maximum project amount has been increased to \$35,000. After reviewing with staff and contractors, I believe some of the cost overruns were the result of attempting to squeeze significant amounts of work into an outdated maximum amount. By increasing the maximum per house by \$10,000, inspectors and contractors will be less likely to leave out items which later become necessary to complete and thus result in change orders and cost overruns. Additionally, projects experiencing significant change orders or cost overruns will be reviewed during monthly financial meetings.

The Division reviewed whether to adjust the contingency amount but does not intend to make any change. While adjusting the amount would potentially reduce the number of cost overruns, it could also result in contractors submitting even more change orders because they know a larger contingency is available. I prefer to better manage the change order process and track the causes of cost overruns while acknowledging that, when working with older homes, some cost overruns are going to be unavoidable.

### **Follow-Up Detail Results:**

**We verified that the revised Rehab Program Policies & Procedures require the approval of all change orders by the Director of Grants & Special Programs, and that each change order must clearly indicate the reason for the change. Testing of**



a sample of change orders verified that they included detailed explanations for the reason(s) for the change orders, and the Grants Director had signed off on the change orders to indicate his review and approval. The Director stated that change orders are also discussed in weekly meetings.

The Director informed us that soon after he became Director he met with the contractors and explained that if they performed any additional work before a change order was approved, they would not get paid for the extra work. He said there have been no change order problems with the contractors.

The maximum project amount has been increased to \$35,000.

The finding is resolved.

