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STATE COMPTROLLER



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July 16, 1998

Mr. Joseph Lynch  
Acting Commissioner  
New York State Division of Housing  
and Community Renewal  
Hampton Plaza  
38-40 State Street  
Albany, NY 12207

Re: Report 97-F-2

Dear Mr. Lynch:

Pursuant to the State Comptroller's authority as set forth in Section 1, Article V of the State Constitution and Section 8, Article 2 of the State Finance Law, we have reviewed the actions taken by officials of the New York State Division of Housing and Community Renewal (DHCR) as of May 31, 1998 to implement the recommendations contained in our prior audit report 92-S-86. Our prior report, issued March 29, 1995, was entitled "Oversight of Mitchell-Lama Housing Replacement Reserves."

**Background**

DHCR plays a central role in formulating State policy for housing development and financing, maintaining the State's low-and middle-income housing stock, and providing technical assistance to communities for housing and community revitalization. Among DHCR's specific responsibilities is the supervision of the Mitchell-Lama Housing program. DHCR's Office of Housing currently oversees the operations of 242 Mitchell-Lama housing projects (project) consisting of 94,670 housing units. Of these projects, 133 projects were financed with bonds issued through the New York State Housing Finance Agency (HFA) and the New York State Housing Loan Fund. The other 109 projects were financed by New York State Urban Development Corporation bonds. Housing companies, which manage the projects, are required to maintain a Operating Escrow Fund (OEF) bank account for monthly escrow and reserve funds. Escrow funds are set aside for insurance, real estate taxes and water and sewerage. Reserve funds are set aside for capital replacements, painting and decorating, and contingencies.

## **Summary Conclusions**

Our prior audit contained recommendations for improving the projects' compliance with the building survey requirements, and using these surveys to better establish reserve requirements for housing companies. We also made recommendations to improve controls over the projects' OEF accounts. In our follow-up review, we found that DHCR has made progress in implementing some of our prior audit recommendations.

## **Summary of Status of Prior Audit Recommendations**

Of the 11 prior audit recommendations, DHCR has fully implemented 3, partially implemented 3 and not implemented 5 recommendations.

## **Follow-up Observations**

### **Recommendation 1**

*Ensure that the surveys are completed, submitted and approved on a timely basis for all projects, including HUD projects.*

Status - Partially Implemented

DHCR Action - DHCR has instituted a system and is progressing toward ensuring that a physical condition survey is completed, submitted and approved for all for projects. At the time of our prior audit, 59 surveys were completed and 52 had been approved by DHCR for the HFA projects. As of May 31, 1998, 116 surveys were completed and 83 of these had been approved.

Auditors' Comments - While there has been improvement in this area we urge DHCR to ensure that surveys are completed and approved for all projects.

### **Recommendation 2**

*Designate responsibility for final approval of surveys, issue a letter to document approval, and centralize recording of surveys.*

Status - Fully Implemented

DHCR Action - DHCR officials have assigned the Architectural and Engineering Bureau (AEB) the responsibility for the final approval of the surveys and the issuance of a letter to document the approval. Also, the AEB has been designated to maintain a centralized data base for the physical condition surveys.

### **Recommendation 3**

*Utilize the results of the approved building surveys to determine the companies' reserve funding requirements.*

Status - Fully Implemented

DHCR Action - DHCR officials have used the results of approved surveys to determine the companies' funding requirement. They state that they will continue to temper such implementation in the rent structure where in their judgement a resultant increase in a development's rents would unduly impact on the tenants and possibly render a housing development unmarketable.

**Recommendation 4**

*Take appropriate action to require compliance with the regulation that companies adequately fund the replacement, painting and decorating, and contingency reserves.*

Status - Not Implemented

DHCR Action - DHCR officials agree with the recommendation that the companies should be required to adequately fund their reserves. They recognize the need and responsibility to take appropriate action when a company is not making reserve deposits despite having funds available to do so.

Auditors' Comments - The reserves are dramatically unfunded for many of the projects. If the companies do not adequately fund the reserves and the projects cannot make necessary repairs, state funds may be required to assist these projects. DHCR must use their resources to ensure that the project reserves are fully funded.

**Recommendation 5**

*Reconcile all OEF account balances annually with the respective bank account balances to verify the accuracy of the OEF cash and investment balances.*

Status - Fully implemented

DHCR Action - DHCR officials have developed a process to reconcile the OEF account annually. Managerial staff monitor the process closely and send follow-up memorandums to ensure that the reconciliations are performed.

**Recommendation 6**

*Compare OEF account balances annually with the respective company financial statements and resolve large differences.*

Status - Partially Implemented

DHCR Action - DHCR officials stated that they have generally instructed their staff to compare the OEF account balances with the companies' financial statement for deficiencies in reporting requirements. If major differences exist in the balances, DHCR staff is required to contact the company's CPA to pursue them.

Auditors' Comments - While the procedure is improved, our test of the 1996 financial statements for four of the ten projects we originally reported on revealed that when the reviewers did their comparisons and found large differences they were not reported to management.

### **Recommendation 7**

*Take appropriate action to ensure that all companies submit complete financial statements on a timely basis.*

Status - Not Implemented

DHCR Action - DHCR's accountants send letters requesting overdue financial statements twice a year. However, our analysis shows that this process is not adequate to ensure that all companies submit complete financial statements on a timely basis. For example, for financial statements that are due in December and the following March, it takes 90 days and 180 days respectively to send the letters. Of 17 statements due in December 1996, none were received as of April 1997. DHCR officials indicate that automation of the budget rent determination system will help address this problem.

Auditors' Comments - We continue to believe that improvements in processes are needed to ensure that companies submit complete financial statements on a timely basis.

### **Recommendation 8**

*Prepare summary reports on the status of the OEF accounts for all the projects.*

Status- Not Implemented

DHCR Action - DHCR officials state that they concur regarding the benefit of generating summary reports on the status of the OEF accounts for all the developments. They anticipate that this will be operational by September 1998.

Auditors' Comments - We continue to believe that this recommendation is important. Without summary reports upper management must rely on staff to report individual problem projects.

### **Recommendation 9**

*Develop a comprehensive procedures manual for the monitoring of the OEF accounts, and distribute the manual to all concerned staff for use.*

Status- Not Implemented

DHCR Action - DHCR officials have developed written procedures for clerical staff covering the disbursement of the escrow and reserve funds from the OEF accounts. However, they stated that other priorities have prevented them from completing a comprehensive manual.

Auditors' Comments - Without a comprehensive procedures manual, DHCR cannot be assured that their staff are familiar with and are following proper and consistent procedures.

**Recommendation 10**

*Establish criteria which better describe or identify items qualifying for disbursement from the replacement reserve funds. When necessary, ensure that DHCR staff adequately document the basis for their decision.*

Status - Not Implemented

DHCR Action - DHCR officials disagreed with this recommendation, stating that to establish criteria would hamper DHCR's ability to address the individual needs of the companies. They believe that eliminating the ability to address company needs as they arise at the operational level would have an adverse impact on the portfolio.

Auditors' Comments - We continue to believe that this recommendation is important. Without established criteria for these disbursements, too much is left to the judgement of the staff and DHCR management cannot be assured that proper and uniform procedures are being followed.

**Recommendation 11**

*Recover from project operating funds all charges determined to be inappropriate to the replacement reserve funds of our sampled projects.*

Status - Partially Implemented

DHCR Action - DHCR officials disagree with \$71,953 of the \$89,726 disbursements that our audit report classified as inappropriate replacement reserve items. They believe that only \$17,773 of the disbursements were inappropriate and these expenditures were reimbursed. For the Saratoga replacement reserve, \$1,766 was reimbursed from the company operation account in February 1994. For the Earl S. Baird Hall replacement reserve, \$16,007 was transferred from the contingency reserves to the replacement reserve in January 1995.

Auditors' Comments - We urge DHCR staff to recover from project operating funds all reserve funds that the companies inappropriately spent on operating costs.

Major contributors to this report were Tom Trypuc, Keith Murphy and Claude Volcy.

We would appreciate your response to this report within 30 days, indicating any additional action you have planned or have taken to address the unresolved matters discussed in this report. We also thank the management and staff of DHCR for the courtesies and cooperation extended to our auditors during this review.

Very truly yours,

Jerry Barber  
Audit Director

cc: Robert King  
Jack Solodow