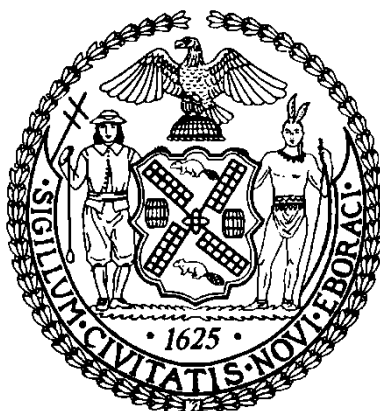


CITY OF NEW YORK OFFICE OF THE COMPTROLLER

**John C. Liu
COMPTROLLER**

MANAGEMENT AUDIT

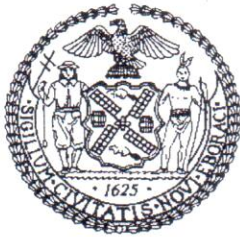
**Tina Kim
Deputy Comptroller for Audit**



Audit Report on the Oversight of the Housing Lottery by the Department of Housing Preservation and Development

MG12-057A

July 19, 2012



THE CITY OF NEW YORK
OFFICE OF THE COMPTROLLER
1 CENTRE STREET
NEW YORK, N.Y. 10007-2341

John C. Liu
COMPTROLLER

July 19, 2012

To the Residents of the City of New York:

My office has audited the Department of Housing Preservation and Development (HPD) to determine whether the housing lottery process is adequately monitored. We audit City processes such as this as a means of ensuring that applicants for City programs are treated fairly.

The audit found that HPD needs to improve controls over its housing lottery process to ensure that only eligible applicants are selected for housing. In addition, HPD does not ensure that Project Managers (PMs) are properly monitoring the developers for assurance that applicants are provided housing based on eligibility. Furthermore, HPD's Marketing Unit has not established policies and procedures to ensure that its complaint resolution process pertaining to the housing lottery is fully documented and has no assurance that all such complaints are resolved.

To address these issues, the audit made seven recommendations, including that HPD: assume the responsibility for selection of applications for the affordable units by developing an automated process for listing and randomly selecting applicants; ensure that PMs conduct required audits and site visits; and develop formal written operating procedures governing the handling of complaints.

The results of the audit have been discussed with HPD officials, and their comments have been considered in preparing this report. Their complete written response is attached to this report.

If you have any questions concerning this report, please e-mail my audit bureau at audit@comptroller.nyc.gov.

Sincerely,

A handwritten signature in dark ink, appearing to read "JCL".

John C. Liu

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***The City of New York
Office of the Comptroller
Management Audit***

**Audit Report on Oversight of the Housing Lottery by the
Department of Housing Preservation and Development**

MG12-057A

AUDIT REPORT IN BRIEF

The New York City Department of Housing Preservation and Development (HPD) works with private, public, and community partners to strengthen neighborhoods and enable more New Yorkers to become homeowners or to rent well-maintained, affordable housing. To accomplish this goal, HPD enters into agreements with developers who are required to construct or rehabilitate residential buildings. In return for obtaining these properties at a fraction of the cost, the developers are required to sell or rent to the public a certain number of units within the dwelling complex at an affordable. Because demand for the units exceeds supply, the lottery system was seen as the preeminent method for resolving issues of accessibility, transparency, and fairness in the selection of tenants or owners applying for affordable housing.

According to HPD's marketing report, a total of 21 projects were completed with application deadlines for Fiscal Year 2011. These 21 projects consisted of 686 available units, of which 681 units were designated as rentals and five units were designated for sale¹.

This audit determined whether HPD adequately monitors the housing lottery process.

Audit Findings and Conclusions

Our review found that HPD needs to improve controls over its housing lottery process to ensure that only eligible applicants are selected for housing. Specifically, HPD has not implemented the recommendations made in a previous audit report pertaining to the creation of a system that allows for the automated filing and selection of applications so as to prevent certain applicants from receiving preferential treatment. We also found that HPD does not ensure that Project Managers (PMs) are properly monitoring the developers for assurance that applicants are provided housing based on eligibility. Furthermore, HPD does not ensure that its PMs consistently conduct required audits and site visits to verify that the applicant selection process is fair and equitable. Moreover, HPD's Marketing Unit has not established policies and procedures to ensure that its complaint resolution process pertaining to the housing lottery is fully documented and has no assurance that all such complaints are resolved.

¹ As of October 2011, 566 of the units had been rented and four units had been sold.

On a positive note, we found that the developers maintained key documents concerning the lottery process.² We also found that the developers verified whether applicants' incomes were within the established income thresholds and that the developers submitted the completed Applicant Information Forms (AIF) to HPD following the applicant interviews. However, these positive aspects are mitigated by HPD's inadequate controls over the applicant selection process.

We did not find instances where unqualified applicants were awarded affordable units and we did not uncover instances of actual fraud. However, the weak controls create an environment where there is an increased risk that errors or fraud may occur and remain undetected. This can occur at the expense of eligible applicants who may lose out on the opportunity to receive affordable housing.

Audit Recommendations

To address these issues, we make seven recommendations, including that HPD should:

- Continue with its quest for an automated process so as to allow applications for housing to be filed online as well as by mail.
- Assume the responsibility for selection of applications for the affordable units by developing an automated process for listing and randomly selecting applicants and incorporating appropriate segregation of duties and supervisory oversight into this process.
- Ensure that PMs adhere to its guidelines and conduct the required audits and site visits of the developers' selection procedures.
- Develop formal written operating procedures governing the handling of complaints.
- Ensure that all complaints and all fields in its spreadsheet are consistently updated with essential information to allow for tracking and following up of complaints.

Agency Response

HPD officials agreed to implement five of the seven recommendations cited in the report. While it appears that HPD officials intend to implement the other two recommendations, they did not directly address all aspects of those recommendations (incorporation of appropriate segregation of duties and supervisory oversight into the automated lottery process as well as ensuring that PMs adhere to guidelines regarding the conduct of audits). In addition, HPD's response included objections to some of our findings. After carefully reviewing the arguments in the response, however, we see no reason to alter our findings.

² The key documents maintained by the developers are as follows: Notice of Intent, marketing meeting notes, sign-in sheet for the marketing meeting, project advertisement, lottery log, lottery sign-in sheet, applicant information forms, spreadsheets containing applicant information, and various e-mails to HPD concerning the projects.

INTRODUCTION

Background

As the nation's largest municipal housing agency, HPD works with private, public, and community partners to strengthen neighborhoods and enable more New Yorkers to become homeowners or to rent well-maintained, affordable housing. To accomplish this goal, HPD enters into agreements with developers who are required to construct or rehabilitate residential buildings. In return for obtaining these properties at a fraction of the cost, the developers are required to sell or rent to the public a certain number of units within the dwelling complex at an affordable price. Because demand for the units exceeds supply, the lottery system was seen as the preeminent method for resolving issues of accessibility, transparency, and fairness in the selection of tenants or owners applying for affordable housing.

HPD's Marketing unit oversees the marketing of affordable housing units as well as the lottery process. The project developer is required to place an advertisement in three newspapers,³ informing the public that applications will be accepted for the advertised project for a period of 60 days. All applications are required to be submitted by the due date to a designated post office box listed in the advertisement. Approximately seven to 10 days after the application deadline, applications are to be picked up by the developer and by an HPD PM and then transferred to the site where the lottery drawing is scheduled to take place.

The lottery is a manual process, whereby the applications are thrown on the floor, mixed up by the developers' staff, and then placed into large, opaque, black plastic bags. Subsequently, staff is required to randomly select applications from each of the plastic bags and enter the selected applications into the log sheets in groups of 10⁴. The applications are to be in full view of the PM, who is prohibited from leaving the site for the duration of the lottery process. The developer is then responsible for interviewing the selected applicants. During the interview, the developer records the applicant's income, family size, and preferences onto an AIF. Afterwards, the developer is required to verify this information, perform background and credit checks, and submit the AIF to HPD for approval prior to renting or selling a unit.

According to HPD's marketing report, a total of 21 projects were completed with application deadlines for Fiscal Year 2011⁵. These 21 projects consisted of 686 available units, of which 681 units were designated as rentals and five units were designated for sale⁶.

³ The three newspapers must be citywide, local, and ethnic. The ethnic newspaper must be for a language that is predominantly spoken in the community board where the project is located.

⁴ The applicant's name, address, household members, relationship to applicant, applicant income, and preference categories are entered onto the log sheets.

⁵ These 21 projects were only funded by HPD as opposed to an additional 23 projects, which were jointly funded by HPD and HDC.

⁶ As of October 2011, 566 of the units had been rented and four units had been sold.

Objective

The objective of this audit was to determine whether HPD adequately monitors the housing lottery .

Scope and Methodology Statement

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. This audit was conducted in accordance with the responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The primary scope of this audit was Fiscal Year 2011. In an effort to confirm whether HPD implemented controls after our scope period, we extended certain aspects of our tests to include lotteries that were conducted through November 2011. Please refer to the Detailed Scope and Methodology at the end of this report for the specific procedures and tests that were conducted.

Discussion of Audit Results

The matters covered in this report were discussed with HPD officials during and at the conclusion of this audit. A preliminary draft report was sent to HPD officials and discussed at an exit conference held on May 15, 2012. We submitted a draft report to HPD officials with a request for comments on May 21, 2012. We received a written response from HPD officials on June 5, 2012. In their response, HPD officials agreed to implement five of the seven recommendations cited in the report. While it appears that HPD officials intend to implement the other two recommendations, they did not directly address all aspects of those recommendations (incorporating appropriate segregation of duties and supervisory oversight into the automated lottery process and ensuring that PMs adhere to guidelines regarding the conduct of audits). In addition, HPD's response included objections to some of our findings. Specifically, HPD officials stated:

“It is our position that many of the report’s findings and general comments (a) are not grounded in real instances and are seemingly hypothetical; (b) neglect the considerable additional measures, some already implemented and others well underway...which continue to enhance procedural controls; and (c) ignore the regulatory structures which already exist and which create a strong compliance environment.”

We disagree with HPD's arguments for several reasons. Regarding point (a), an audit is intended to identify, among other things, deficiencies that increase the risk that improprieties or fraud *could* occur. The significance of an identified deficiency is not necessarily dependent on whether or not the potential impropriety or fraud actually occurs as implied by HPD. For example, cash stored in an open, unguarded safe is vulnerable to theft. Under HPD's logic,

however, this would not constitute a significant deficiency unless one had evidence of an instance in which cash had been stolen. Regardless of whether or not we detected any specific instances of fraud or irregularities, the fact remains that the weaknesses we identified in HPD's oversight increases the risk that such instances could occur and go undetected. HPD management acknowledged this during our exit conference and it is discernable throughout HPD's response. The agency clearly recognizes the need for a more detailed method of oversight and has agreed to implement most of our recommendations.

Regarding point (b), many of the procedural changes cited by HPD in its response were not in effect during the audit scope period (Fiscal Year 2011), but were instituted subsequent to our informing HPD in July 2011 of our intent to engage this audit and often after we raised these issues with HPD officials. Additionally, the additional measures cited by HPD throughout its response merely highlights the fact that HPD officials are aware that additional precautionary measures were required on their part and serves to contradict their attempt to minimize the significance of our findings.

Finally, regarding point (c), HPD did not provide us with any evidence during the course of this audit to support its current argument that the monitoring activities of other regulatory agencies reduced the need for HPD to maintain its own comprehensive system of controls over the housing lottery and applicant selection process. Absent such evidence, we focused solely on the controls developed by the Marketing Unit, which fall short of what we would expect to observe in an adequate control environment. In addition, notwithstanding the roles of third parties such as the New York City Housing Development Corporation, the U.S. Department of Housing and Urban Development, and the U.S. Internal Revenue Service, HPD either plays or should play an integral role in the housing lottery and applicant selection process and cannot afford to be lax in developing its own controls.

Based on the above, we see no reason to alter our findings. The full text of the HPD response is included as an addendum to this report.

FINDINGS AND RECOMMENDATIONS

HPD needs to improve controls over its housing lottery process to ensure that only eligible applicants are selected for housing. Specifically, HPD has not implemented the recommendations made in a previous audit report pertaining to the creation of a system that allows for the automated filing and selection of applications so as to prevent certain applicants from receiving preferential treatment.

HPD does not ensure that PMs are properly monitoring the developers for assurance that applicants are provided housing based on eligibility. Namely, HPD only verifies income-related supporting documentation and does not verify all other supporting documents to ensure applicant eligibility. In addition, HPD does not verify whether those applicants who had been denied housing did not actually qualify. Furthermore, HPD does not ensure that its PMs consistently conduct required audits and site visits to verify that the applicant selection process is fair and equitable. Moreover, HPD's Marketing Unit has not established policies and procedures to ensure that its complaint resolution process pertaining to the housing lottery is fully documented and has no assurance that all such complaints are resolved.

On a positive note, we found that the developers maintained key documents concerning the lottery process.⁷ We also found that the developers verified whether the applicant's income was within the established income thresholds and that the developers submitted the completed Applicant Information Forms (AIF) to HPD following the applicant interviews. However, these positive aspects are mitigated by HPD's inadequate controls over the applicant selection process.

We did not find instances where unqualified applicants were awarded affordable units and we did not uncover instances of actual fraud. However, the weak controls create an environment where there is an increased risk that errors or fraud may occur and remain undetected. This can occur at the expense of eligible applicants who may lose out on the opportunity to receive affordable housing.

The details of these findings are discussed in the following sections of this report.

Lack of Policies and Procedures to Ensure Eligibility of All Applicants

HPD has not created adequate policies to ensure that only eligible applicants are selected from the lottery process and are offered affordable housing. As a result, there is a possibility for ineligible applicants to receive a preference for housing.

⁷ The key documents maintained by the developers are as follows: Notice of Intent, marketing meeting notes, sign-in sheet for the marketing meeting, project advertisement, lottery log, lottery sign-in sheet, applicant information forms, spreadsheets containing applicant information, and various e-mails to HPD concerning the projects.

Insufficient Controls with the Applicant Selection Process

The manual housing lottery process that HPD currently uses to select applicants for interviews to determine eligibility for affordable housing needs improvement. Specifically, manually selecting applications can result in some applicants being unfairly denied an opportunity to be selected for an interview. In addition, it increases the potential for applicants to receive preferential treatment.

The basic premise of the lottery process is for applications to be randomly selected so that all applicants have an equal opportunity of being selected. However, the current process of placing all of the applications on the floor, manually mixing them up, and placing them into plastic bags so that project developer staff can select and log the applications onto a log sheet is antiquated and not sufficiently random. Because the selection process is not automated and is exclusively dependent on the involvement of the developer's staff, an applicant known to the developer or his staff can be systematically selected and logged high on the log sheet. There also exists the risk that the developer or his staff can add an applicant who has not submitted an application on time. In both of these scenarios, the favored applicant would have a greater opportunity over other applicants for receiving the limited and desired space in one of the affordable housing units. HPD officials place great reliance on the PMs' presence during the lottery process as a control to prevent improprieties from occurring. However, this alone is not a sufficient control, especially in the case of larger lotteries, where one PM is charged with the responsibility of overseeing thousands of applications processed by 20 to 30 staff.

HPD Response: "...representatives from HPD and The New York City Housing Development Corporation (HDC) monitor every developer and/or marketing agent through the lottery process."

Auditor Comment: Only one HPD PM (and no HDC official) was present at the two lotteries we observed. This level of oversight is insufficient, especially for large projects, and increases the possibility for collusion between the developer and the PM.

During our own observations of the housing lottery process, we systematically selected a sample of 100 applicants to verify whether the addresses were accurately recorded to capture the community board status. Because applicants residing in the specified community board are offered first preference, the correct classification of these applicants is essential to the integrity of the process. We found two instances (out of 11 community board residents in our sample⁸) where the applicants were erroneously marked as community board residents. It appears that the PM had inadvertently marked the lottery log to indicate that the applicant resided in the community board where the project was based⁹.

⁸ We randomly selected a sample of 100 applicants to review their community board status, of which 11 applicants were marked as belonging to the community board of that particular lottery.

⁹ During the housing lottery process, it is the PMs' responsibility to verify whether, based on the address listed on the application, the applicant belongs to the community board of that project and to list that information on the log sheet.

The current use of a manual process means that the integrity of the housing lottery process relies predominantly on the integrity of the individuals conducting the housing lottery. Moreover, it leaves the possibility open for the risk that fraud can occur during the selection process. A previous audit report issued by our office on August 5, 2009 (*Audit Report on the Department of Housing Preservation and Development Cornerstone Program*, #ME09-077A), cited HPD for these same deficiencies. The previous audit recommended that HPD should consider automating the housing lottery process by making it possible to complete the application online or through the 311 telephone system. HPD agreed to explore the feasibility of using other options to select applicants and is currently devising a plan for an automated system with a targeted release date of August 2012.

Recommendations

HPD should:

1. Continue with its quest for an automated process so as to allow applications for housing to be filed online as well as by mail.

HPD Response: “The automated system, NYC Housing Connect, launched on June 5th with two projects. The full roll out is expected in the fall of 2012.”

2. Assume the responsibility for selection of applications for the affordable units by developing an automated process for listing and randomly selecting applicants and incorporating appropriate segregation of duties and supervisory oversight into this process.

HPD Response: “HPD developed and launched an online application system that allows the agency to electronically randomize the lottery process and exercise more efficient control over the distribution and review of the lottery list. However, we must point out that the agency cannot ‘assume the responsibility for selection of applicants...’ through this or any other process. It is still the responsibility of the owner/developer to screen applicants for eligibility under HPD’s or HDC’s oversight. ... The automation, along with all the other measures detailed throughout this response, will enhance our control of that process.”

Auditor Comment: We are pleased that HPD has agreed to implement part of our recommendation to develop an automated process for listing and randomly selecting applicants. However, HPD has not addressed the second part of the recommendation pertaining to the incorporation of appropriate segregation of duties and supervisory oversight into this process. In its response, HPD refers to the responsibility of the owner/developer to screen applicants – a process that occurs *after* applicants are selected through the lottery drawing. The focus of this recommendation is on the segregation of duties and supervisory oversight that occurs *during* the actual lottery drawing. We urge HPD to also implement this part of the recommendation.

Insufficient Controls to Ensure Applicants' Eligibility

HPD has not implemented sufficient controls to ensure that only eligible applicants are selected for the limited units. Specifically, HPD has not established adequate policies and procedures to verify all aspects of eligibility and conversely, the ineligibility of those applicants denied. This includes a lack of audits and site visits to review the selection process. By not verifying the eligibility as well as ineligibility of applicants, HPD is forced to rely on the integrity of the developer. In doing so, HPD is left vulnerable to the potential of fraud occurring on the part of the developer. Applicants selected first in the lottery process may be unfairly denied the opportunity to obtain affordable housing in favor of applicants preferred by the developer who are subsequently selected.

Inadequate Review and Verification of Supporting Documents

The review of supporting documents prior to the approval of applicants is a critical aspect of the application process that all developers must undertake. This consists of the developer reviewing an applicant's proof of income, which until September 2011 – two months after the start of our audit and two years since the issuance of the previous audit report – did not have to be independently verified. Since then, HPD implemented procedures to verify that only applicants who satisfy the income requirements are selected for the marketed units¹⁰. However, HPD verifies income only for those applicants deemed eligible by the developer. HPD does not take sufficient steps to ascertain whether those applicants who have been disqualified by the developer were appropriately rejected. As a result, there is an increased risk that the developer may intentionally deem qualified applicants as ineligible in order to select those applicants preferred by the developer. HPD officials stated that rejected applicants have an opportunity to voice their concerns via the appeals process at which time HPD reviews the applicant's entire file. However, this occurs after the fact and is not a preventive measure to help ensure that all applicants are offered equal opportunities.

HPD Response: “Measures implemented as part of that initiative to date include the following: ... 2. The implementation of a pre-audit process where HPD and HDC review applicants deemed eligible by the developer and/or marketing agent prior to the final approval.”

Auditor Comment: In its response, HPD places a great deal of emphasis on reviewing the files for eligible applicants, while ignoring the potential risk that developers may deliberately deem applicants as ineligible so as to select preferred applicants. In an effort to ensure that all applicants have an equal opportunity to be selected for housing and only ineligible applicants are disqualified, HPD should review supporting documents pertaining to all applicants – those deemed eligible as well as those deemed ineligible.

¹⁰ Along with the AIF, the developers are now required to submit to HPD the Tenant Income Certification, which is completed by the developer; the IRS Form 4506-T, which is completed by the applicant and allows the IRS to release transcripts directly to third parties; and the Third Party Verification, allowing developers to obtain income information directly from the applicant's employer.

In addition to the verification of income, developers are also required to verify the applicant's assets, family composition, and address as well as perform a criminal background and credit history check, and investigate previous landlord/tenant disputes. However, other than the review of documents to verify income, HPD does not review any other evidence to ensure that the developer verified any of the other information cited above. As a result, HPD is hindered in knowing whether applicants approved for housing were actually eligible and whether those denied were inappropriately rejected. HPD also has limited ability to ascertain whether an element of fraud or collusion exists between the developer and the applicants.

Lack of Audits and Site Visits to Ensure Eligibility of Applicants

According to HPD's policies and procedures, PMs are required to audit the selection process of applicants approximately 30 days after the completion of the lottery. PMs are also required to conduct periodic visits to the developer's site. These audits and site visits are an essential part in ensuring that applicants are selected in accordance with HPD's guidelines. Specifically, in an effort to ensure that eligible applicants are selected, PMs are required to review the household size, income eligibilities, and third party verifications.

During Fiscal Year 2011, HPD completed 21 projects with application deadlines during that year. However, none of the five PMs conducted any audits that year and only two of the five PMs performed site visits for three of the 21 projects¹¹. As a result, HPD has little, if any, assurance that only eligible applicants were selected for these projects. Moreover, contrary to its procedures, one of these visits took place seven months after the completion of the lottery process (the other PM made visits that were between three months and six months after the lottery process). According to an HPD official, site visits were intended to be conducted on a regular basis, but over time, the review process evolved into an "as needed" or "if necessary trouble-shooting activity." However, the lack of effective monitoring of the selection process poses a potential risk that fraud or errors can occur without being detected in a timely manner. In addition, HPD does not provide a standardized format for PMs to document any concerns noted during their observations. In fact, the two PMs who did perform site visits hand-wrote their observations and never formally documented the types of documents they reviewed during the site visits.

Audits and site inspections are an integral part of an internal control structure, whereby management can ensure that goals and objectives are achieved. A formal review process would help promote consistency among PMs during their reviews and provide more transparency as to what the reviews actually entail. Without it, neither we nor HPD have adequate assurance that only eligible applicants are selected.

The lack of some of these procedures or ineffectiveness of those controls that are in place may put applicants at risk of being unfairly and unjustly denied the opportunity to receive affordable housing. In fact, the shortage of effective controls and measures results in the undermining of one of the goals of the program – which is to provide for affordable homes to eligible New Yorkers. Many program participants have modest incomes and rely on the City to assist them in realizing their goals. As such, it is essential for the program to be conducted

¹¹ One PM visited two projects three times for each project. The second PM visited one project one time.

effectively and efficiently, so that all eligible applicants have an equal and viable opportunity to be selected for affordable housing. In the absence of controls and measures by HPD, the overall goal of the program may be severely hindered.

HPD Response: “The implementation of enhanced and integrated HPD-HDC Marketing Guidelines, formatted for the first time as an extensive manual...The extensive, detailed content of this manual marks a major achievement in that it creates a formal resource of information for developers to follow throughout each step of the process to avoid mistakes.”

Auditor Comment: While we applaud HPD for the creation of this manual, HPD’s lack of audits and site visits inhibits the ability of HPD management to ensure that developers are adhering to those guidelines.

Recommendations

HPD should:

3. Ensure that PMs adhere to its guidelines and conduct the required audits and site visits of the developers’ selection procedures.

HPD Response: “In September of 2011 the agency initiated a policy of full compliance review for a minimum of 20% of applicants submitted by the developer to the agency for approval and selected at random. The compliance review has a checklist of required documents. Also, all projects are required to submit support documents in addition to the Applicant Information Form (AIF). ... HPD will also ensure that site visits are conducted in a proactive manner and not only on an ‘as needed basis’.”

Auditor Comment: Although it appears that HPD has agreed to implement this recommendation, there are certain aspects that are either unclear or not addressed in its response. While it is commendable that HPD intends to conduct audits and site visits, it must ensure that audits are conducted in accordance with its policies and procedures, which requires an audit of the selection process of applicants approximately 30 days after the completion of the lottery.

In addition, HPD refers to supporting documents that must be submitted in addition to the AIF. HPD does not identify these supporting documents in its response, but it did provide us with a listing during the course of our audit. The documents in that listing relate only to income verification. However, developers are also required to verify the applicant’s family composition and address, as well as perform criminal background and credit history checks and investigate previous landlord/tenant disputes. We found no evidence that HPD requires that developers submit supporting documentation pertaining to these tasks. As such, we believe it would be in HPD’s best interest to review those documents as well to help ensure that only eligible and qualified applicants are ultimately approved.

4. Develop a checklist or a standard document to record the results of the audits and visits as well as any subsequent follow-up action.

HPD Response: “HPD will develop the site visit checklist for all project managers to use and will implement it by August 1, 2012.”

Auditor Comment: While it is commendable that HPD intends to develop site visit check lists, HPD should ensure that its audit results and subsequent follow-up actions are documented as well.

Lack of Policies and Procedures to Resolve Complaints

HPD’s Marketing Unit has not established sufficient policies and procedures for tracking and handling complaints from applicants regarding the selection process of affordable housing. This can reduce the Marketing Unit’s ability to monitor and resolve complaints.

Although the Marketing Unit maintains that it tracks, investigates, and resolves complaints pertaining to the lottery process, the mechanism used for processing the complaints is inadequate. Currently, the Marketing Unit does not ensure that all necessary information required to address the complaints is noted for each complaint recorded on its electronic spreadsheet. To one degree or another, the name and address of the complainant, the name of the PM responsible for follow-up, the name of the project, the name of the developer, and the resolution of the complaint are not consistently recorded on the spreadsheet, thereby preventing the Marketing Unit from using it for any type of meaningful trend analysis concerning the types of complaints made or their resolutions .

In fact, of the 220 entries that we reviewed¹², none of them listed in the designated space for these entries the PM responsible for investigation and follow-up of the complaints. Furthermore, 100 of the complaints did not capture the complainant’s name and instead listed an e-mail address in the field designated for the name of the complainant. While we acknowledge that complainants may not initially provide all personal information, the PM can update these fields during the course of the investigation of the complaint. The inconsistent recording of vital information necessary for complaint resolution reduces the effectiveness of the spreadsheet as a monitoring device. In its current state, HPD’s Marketing Unit cannot readily offer information to applicants who make inquiries concerning the status of a complaint nor can the Marketing Unit identify those developers who have the greatest number of complaints made against them because neither piece of information is consistently recorded.

In addition, we found a total of 10 complaints that had been forwarded by HPD’s Commissioner’s Office to the Marketing Unit for follow-up that were not even listed as complaints in the Marketing Unit’s electronic spreadsheet. HPD officials stated that this was an oversight on their part. However, the discrepancy between the two listings not only highlights the fact that the tracking device used by the Marketing Unit is inaccurate, but also that there exists a

¹² The 220 entries that we reviewed consisted of all complaints recorded by the Marketing Unit during Fiscal Year 2011.

possibility that complaints can be overlooked. Although we did not find instances where this was the case, the weak controls create an environment where this can readily occur.

Recommendations

HPD should:

5. Develop formal written operating procedures governing the handling of complaints.

HPD Response: “HPD will follow your recommendation to further tighten our process and will develop a formal written operating procedures document governing the handling of complaints by August 1, 2012.”

6. Ensure that all complaints and all fields in its spreadsheet are consistently updated with essential information to allow for tracking and following up of complaints.

HPD Response: “HPD will populate all the key information provided by the individual generating the complaint into a central tracking chart for marketing and will update it on a regular basis. Your observation about personal information such as the names of the complainants sometimes not being recorded is mitigated by the fact that sometimes complainants wish to remain anonymous not just initially but for the duration of their contact with our staff.”

Auditor Comment: We are pleased that HPD intends to populate and update its central tracking chart with key information. However, we are puzzled by HPD’s comments regarding complainants who wish to remain anonymous; this is the first time that HPD has presented this argument, although it had opportunity to do so when this issue was raised during the course of the audit. Further, HPD has provided no evidence of instances in which complainants’ personal information was not recorded due to complainants’ wishes to remain anonymous and not merely due to its staff’s failure to record this information.

7. Perform an analysis of complaints received to highlight possible areas of concern.

HPD Response: “HPD categorizes the types of complaints received in order to understand what the most frequent issues are. HPD will continue to do so and will perform an analysis of all the complaints received every quarter.”

Auditor Comment: We did not receive any evidence from HPD to support its claim that it categorizes complaints. Nevertheless, we are pleased that, moving forward, HPD intends to analyze the complaints it receives on a quarterly basis.

DETAILED SCOPE AND METHODOLOGY

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was conducted in accordance with the audit responsibilities of the City Comptroller as set forth in Chapter 5, §93, of the New York City Charter.

The primary scope of this audit was Fiscal Year 2011. In an effort to confirm whether HPD implemented controls after our scope period, we extended certain aspects of our tests to include lotteries that were conducted through November 2011.

To obtain an understanding of the methods used by HPD to monitor the housing lottery process, we conducted walk-throughs and interviews with HPD's Marketing unit. Specifically, we interviewed HPD's Director of Marketing and the four project managers¹³. We also interviewed the Executive Director of HPD's Tax Credit Allocations unit to obtain an understanding of the relationship between the low income housing tax credit and the participants in the projects. To gain an understanding of the lottery process, we observed two lotteries - one was conducted from October 7, 2011, through October 14, 2011, and the other was conducted from November 15, 2011, through November 16, 2011. We observed the process from the retrieval of the mail from the United States Postal Service to the time that all applicants' names were entered onto the lottery log sheets. To further understand all aspects pertaining to the lottery process, we interviewed representatives of the two managing agents who conducted the two lotteries.

To obtain an understanding of the methods used by HPD in documenting, tracking, and resolving complaints pertaining to the lottery process, we interviewed the office manager responsible for receiving and distributing the complaints to the respective PMs responsible for the resolution. We reviewed the population of 220 complaints received during Fiscal Year 2011 by the Marketing Unit. To verify the accuracy and completeness of this data, we compared it to the listing of complaints forwarded by the HPD Commissioner's Office to the Marketing Unit, using the tickler number as the common identifying field¹⁴.

To assess the adequacy of HPD's internal controls concerning its monitoring of the housing lotteries, we obtained and reviewed from HPD's website pertinent information pertaining to the process. We also evaluated the responses provided by our interviewees and analyzed various supporting documents. We used HPD's Marketing Guidelines for Renters and Owners as well as HPD's Project Manager Guide as audit criteria. We also reviewed a previous report issued by our office on August 5, 2009 (*Audit Report on the Department of Housing*

¹³ The Marketing Director also acts as a PM for projects with 20 units or less for a total of five PMs.

¹⁴ This is a sequential number issued by the Commissioner's office to track complaints. Initially, all complaints are received by the Commissioner's Office, are assigned a tickler number, and are then forwarded to the respective departments within HPD for follow-up.

Preservation and Development Cornerstone Program, #ME09-077A) and verified whether HPD had implemented the recommendations relevant to the housing lottery process.

To determine the total number of housing lotteries with application deadlines within Fiscal Year 2011, we reviewed the Marketing Report maintained by HPD's Marketing Unit¹⁵. To determine whether the developers maintained supporting documents concerning the housing lottery process, we judgmentally selected five developers with complaints lodged against them out of our population of 220 complaints. We reviewed the housing lottery project folders for key supporting documents, such as the Notice of Intent, the marketing meeting notes, project advertisement, the lottery log, the lottery sign-in sheet, applicant information forms, spreadsheet containing applicant information, and correspondences to HPD concerning the project. We also randomly selected 10 applicants from each of the five lottery logs maintained by the developers to determine whether the developers accurately ascertained whether the applicants' income was within the acceptable income threshold. We compared the applicants' income as reflected in the lottery log to the income guidelines indicated in the advertisement. In addition, we judgmentally selected five applicant folders from each of the five developers and conducted a review of the income verification documents submitted along with the applications. Specifically, we verified whether the applicants submitted the paystubs, employment letter, W-2s, and completed tax returns.

To determine whether the PMs conducted audits and periodic site visits to developer sites to review the progress of the applicant selection process, we reviewed all pertinent notes and supporting documents that were available, such as the handwritten notes completed by the PMs and correspondence between the developers and the applicants. We also verified whether the site visits were recorded in a format that would assist HPD management in determining whether the developer had issues that needed to be addressed.

While some of the above tests involved samples that were not projected to their respective populations, the results of these and other tests that we performed provided a reasonable basis for assessing and supporting our conclusions regarding the adequacy of HPD's monitoring of the housing lottery process.

¹⁵ The report listed all housing lotteries monitored by HPD from the late 1980s to the present.



Department of
Housing Preservation
& Development
nyc.gov/hpd

MATHEW M. WAMBUA
Commissioner

Office of the Commissioner
100 Gold Street
New York, N.Y. 10038

ADDENDUM

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June 5, 2012

Tina Kim
Deputy Comptroller for Audits
Office of the New York City Comptroller
1 Centre Street- Room 1100N
New York, New York 10007-2341

**Re: Audit on the Oversight of the Housing Lottery by the Department of Housing
Preservation and Development
Audit Number: MH12-057A**

Dear Deputy Comptroller Kim:

The following represents the Department of Housing Preservation and Development's response to the findings and recommendations made in your audit on the Housing Preservation and Development's Oversight of the Housing Lottery.

Thank you for your consideration during the fieldwork and at the Exit Conference.

If you have any additional questions, please call Assistant Commissioner Josh Cucchiaro at (212) 863-6610.

Thank you.

Sincerely,

Mathew M. Wambua



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NEW YORK CITY OFFICE OF THE COMPTROLLER
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Thank you for the opportunity to provide comments for inclusion in your report on the housing lottery process audit. The Marketing team follows clear policies and procedures to ensure that affordable housing is being distributed in a fair and equitable manner and we are pleased to read that your extensive audit did not find a single instance of an unqualified applicant being awarded affordable units or fraud.

Given that, we strongly disagree with some of the report's content. It is our position that many of the report's findings and general comments (a) are not grounded in real instances and are seemingly hypothetical; (b) neglect the considerable additional measures, some already implemented and others well underway, which were discussed at length during the audit and which continue to enhance procedural controls; and (c) ignore the regulatory structures which already exist and which create a strong compliance environment.

Your report makes a "positive note" regarding the completeness and accuracy of the lottery records, income verification and other selection procedures implemented by the developers of the audited projects. This level of developer compliance did not and does not occur by accident. Developers and marketing agents are required to comply with the HPD-HDC Marketing Guidelines, per their Regulatory Agreement. Further, representatives from HPD and The New York City Housing Development Corporation (HDC) monitor every developer and/or marketing agent through the lottery process. The audit fails to recognize the controls that are already in place. To this end, the agency would like to stress the following facts:

- All of the 21 projects included in your audit are governed by HPD Regulatory Agreements which dictate compliance with marketing, eligibility and selection requirements. Failing to adhere to those requirements can result in serious consequences, all of which are very well known to the developers, including:
 - o The loss of tax benefits which are tied to the affordability restrictions and can have a significant financial repercussion;
 - o Litigation by The City (with legal costs to be reimbursed by the developer) to ensure specific compliance with regulatory documents;
 - o In cases involving suspicion of fraud, referral to The New York City Department of Investigation (DOI) for criminal review; and
 - o In projects where The City holds a mortgage, a declaration of loan default.

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- Of the 21 audited projects, 17 have HOME funding, were financed with Low Income Housing Tax Credits (LIHTC) or had a combination of both, making these projects subject to federal compliance with HUD and the IRS respectively. The agency has distinct compliance units in our Asset Management and Tax Incentives Departments, separate from our marketing staff, which conduct audits of HOME and LIHTC projects as required by these federal programs. Any non-compliance, whether by accident or intention, discovered during these post-audits can lead to additional and serious consequences at the federal level. These consequences may include the loss of HOME funds and the recapture of tax credits, both of which would have devastating financial impact on the projects and their developers, and referral to HUD's Office of Inspector General and/or the IRS in cases where fraud is suspected.

- Further, for all our LIHTC projects (including 17 of the properties in your audit), there is an additional agency-approved LIHTC investor which oversees the private developers and protects the financial security of the tax credits by providing another layer of compliance monitoring. These entities are in fact required to remain in the limited partnership of each project's ownership structure for a period of 15 years and as such have a major financial stake in protecting the tax credits by ensuring compliance through the monitoring activities of their own, expert staff.

All of the above factors contribute to a network of compliance that the agency has achieved by design, not by accident. The lack of any findings of ineligible approvals or instances of fraud in the audited universe supports the effectiveness of this purposeful structure.

We do acknowledge we could be more proactive in conducting timely site visits to the developers' offices and enhance our current tracking system for complaints. Indeed a great deal of our marketing staff's time has been dedicated to planning and implementing significant procedural changes which were discussed throughout the audit, but neglected in the report. These changes have and will continue to result in a significant enhancement of compliance controls in the process both now and in the future.

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As discussed at great length throughout the audit interviews and process, the agency has undertaken a comprehensive initiative to make substantial improvements in its marketing, lottery and tenant eligibility processes. Measures implemented as part of that initiative to date include the following:

1. *The transition of the marketing team to HPD's Office of Development* in order to unify the coordination of new projects from their planning stage through the completion of their initial occupancy. (Implemented in 2009)
2. *The implementation of a pre-audit process* where HPD and HDC review applicants deemed eligible by the developer and/or marketing agent prior to the final approval.
 - a. For projects jointly financed with HDC, the agency coordinates the marketing process through HDC. Such joint-agency projects comprised approximately 78% of HPD's annual production of new housing in FY11. As a bond finance and compliance agency, HDC performs a 100% pre-audit of applicants deemed eligible. (Implemented in 2009)
 - b. On all other projects, HPD has now dedicated resources in the marketing team to perform a minimum of 20% pre-audit of all applicants deemed eligible. This is a major shift in moving the eligibility audit functions to a pre-audit basis. Twenty percent (20%) has provided the correct balance between (a) managing limited agency resources; and (b) providing a large enough sample to observe potential trends of concern such as repetitive errors by developers in certain income calculations, among others. (Implemented in September 2011)
3. *The implementation of closer coordination with The New York City Department of Investigation (DOI)* in the marketing and leasing process. Any applicant reviewed by HPD who is a municipal worker is submitted to DOI whose investigators then independently verify through the City payroll records that the reported salary information is truthful and accurate. Further, any applicant reviewed by HPD whose documentation appears to our staff to be suspect in any way is shared with our DOI Inspector General for their review and guidance. Warning language on all applications and related forms has been strengthened to emphasize to the public that all documents are subject to DOI review and that

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falsifying or intentionally withholding information to induce eligibility will result in consequences that may include criminal prosecution. (Implemented in April 2008)

4. *The implementation of enhanced and integrated HPD-HDC Marketing Guidelines*, formatted for the first time as an extensive manual, copies of which were provided to your auditors. These guidelines strengthen the lottery review process for developers and formalize income documentation requirements for applicants. The extensive, detailed content of this manual marks a major achievement in that it creates a formal resource of information for developers to follow throughout each step of the process to avoid mistakes. In addition, it further provides uniform documents to be used in evaluating and recording the household income for applicants. Further, the developer of each new project now must submit and have approved its own marketing plan to the agency in advance of the start of the marketing process to create a project-specific record of the marketing strategies and eligibility criteria for each. (Implemented in March 2012)
5. *The automation of the lottery process*. The goal of automating this process has been one the agency has been considering and researching to various degrees for an extended period of time – even prior to the 2009 audit cited in your report. While it may seem like a simple solution, there are many concerns which have required extensive and responsible due diligence. The issues of accuracy, security and capacity needed to be carefully researched and reconciled. We are dealing with sensitive, private information regarding applicants' incomes, disabilities and other household characteristics. There is no room for security mistakes or access flaws. Further, even lotteries conducted via the all-paper process can sometimes draw more than 20,000 applications. It was therefore necessary to ensure system capacity for that kind of volume (and even more anticipating that automation could result in far greater responses) through appropriate stress-testing and simulations. Further, because not all New Yorkers have access to computers, we needed to design a process that allowed for both online and paper applications to be treated equally on the back-end prior to generating the log. We are happy to report that the pilot for the automated housing lottery, NYC Housing Connect, launched on June 5th. Applicants can now apply for two pilot projects via www.nyc.gov/housingconnect. We expect the full roll out to be in the fall so that New Yorkers can apply to all HPD and

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HDC lotteries through the automated system, if they wish to do so. Paper applications will continue to be accepted for all projects. (Implemented in June 2012)

Following are our responses to your specific recommendations.

Finding	Recommendation 1.	Response 1.
Lack of Policies and Procedures to Ensure Eligibility of All Applicants	HPD should continue with its quest for an automated process so as to allow applications for housing to be filed online as well as by mail.	The automated system, NYC Housing Connect, launched on June 5 th with two projects. The full roll out is expected in the fall of 2012. The automation of the marketing lottery has been well under way for several years, as described in detail in discussion during the audit and in writing above.
Finding	Recommendation 2.	Response 2.
Insufficient Controls with the Applicant Selection Process	HPD should assume the responsibility for selection of applications for the affordable units by developing an automated process for listing and randomly selecting applicants and incorporating appropriate segregation of duties and supervisory oversight into this process.	As noted above, HPD developed and launched an online application system that allows the agency to electronically randomize the lottery process and exercise more efficient control over the distribution and review of the lottery list. However, we must point out that the agency cannot "assume the responsibility for selection of applicants..." through this or any other process. It is still the responsibility of the owner/developer to screen applicants for eligibility under HPD's or HDC's oversight. Unlike NYCHA, HPD does not own these buildings. Instead, HPD works with private developers (i.e. landlords) who are ultimately responsible for tenant selection in a manner that complies with agency rules, as required in their Regulatory Agreements. The automation, along with all the other measures detailed throughout this response, will enhance our control of that process.

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Finding

Insufficient Controls
to Ensure
Applicants'
Eligibility

Recommendation 3.

HPD should ensure that PMs
adhere to its guidelines and
conduct the required audits and
site visits of the developers'
selection procedures.

Response 3.

In September of 2011 the agency initiated a policy of full compliance review for a minimum of 20% of applicants submitted by the developer to the agency for approval and selected at random. The compliance review has a checklist of required documents. Also, all projects are required to submit support documents in addition to the Applicant Information Form (AIF). These changes are consistent with policies of other government housing agencies, locally and nationally, and satisfy internal compliance standards with other parts of the agency. With the implementation of this process, the agency has significantly modified its approach to performing *pre-audits* which is clearly a superior application of resources and a preferable control to conducting post-audits and site visits. HPD will also ensure that site visits are conducted in a proactive manner and not only on an "as needed basis".

Finding

Inadequate Review
and Verification of
Supporting
Documents

Lack of Audits and
Site Visits to Ensure
Eligibility of
Applicants

Recommendation 4.

HPD should develop a
checklist or a standard
document to record the results
of the audits and visits as well
as any subsequent follow-up
action.

Response 4.

HPD will develop the site visit checklist for all project managers to use and will implement it by August 1, 2012.

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Finding

Lack of Policies and
 Procedures to
 Resolve Complaints

Recommendation 5.

HPD should develop formal
 written operating procedures
 governing the handling of
 complaints.

Response 5.

We are pleased that your thorough review found no instances where any complaints had been overlooked. HPD will follow your recommendation to further tighten our process and will develop a formal written operating procedures document governing the handling of complaints by August 1, 2012.

Recommendation 6.

HPD should ensure that all
 complaints and all fields in its
 spreadsheet are consistently
 updated with essential
 information to allow for
 tracking and following up of
 complaints.

Response 6.

HPD will populate all the key information provided by the individual generating the complaint into a central tracking chart for marketing and will update it on a regular basis. Your observation about personal information such as the names of the complainants sometimes not being recorded is mitigated by the fact that sometimes complainants wish to remain anonymous not just initially but for the duration of their contact with our staff.

Recommendation 7.

HPD should perform an
 analysis of complaints received
 to highlight possible areas of
 concern.

Response 7.

HPD categorizes the types of complaints received in order to understand what the most frequent issues are. HPD will continue to do so and will perform an analysis of all the complaints received every quarter.

In closing, we appreciate the opportunity to provide our comments. Any procedural system as expansive and volume-intensive as our agency's marketing program will always be subject to challenges whether they are related to staff performance, technology accuracy or merely the availability of resources. The key is to meet those challenges and

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continuously strive for improvement on all levels. We have already met many of the recommendations observed in your report and implemented applicable improvements. We will continue to make changes that enhance the agency's controls over ensuring affordable housing in New York City is distributed in an equitable and fair manner.