



WENDY GREUEL
CONTROLLER

June 15, 2010

City Council
c/o City Clerk
Room 395, City Hall

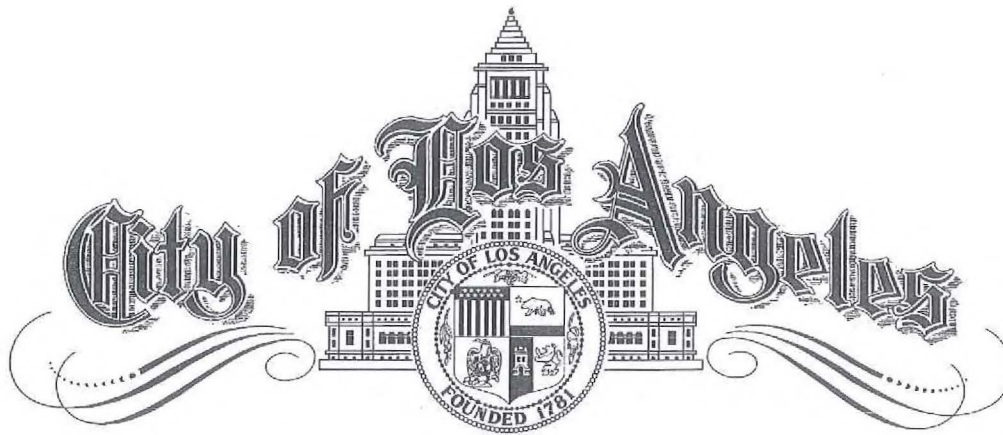
Dear Honorable Members of the City Council:

Attached, please find follow up correspondence to the report entitled "Review of LAHD's Selection and Award to Bonnie Brae Village Housing Project for the 2007 Permanent Supportive Housing Program" released earlier this year (C.F. 10-0626).

Sincerely,

A handwritten signature in cursive script, appearing to read "Wendy Greuel", is written in dark ink.

WENDY GREUEL
City Controller



OFFICE OF
CONTROLLER

200 N. MAIN STREET, RM 300
LOS ANGELES 90012
(213) 978-7200
www.lacity.org/ctr

June 14, 2010

Douglas Guthrie, General Manager
Los Angeles Housing Department
1200 West 7th Street, 9th Floor
Los Angeles, CA 90012

Dear Mr. Guthrie:

**SUBJECT: EVALUATION OF LAHD'S RESPONSE TO REPORT TITLED
"REVIEW OF LAHD'S SELECTION AND AWARD TO BONNIE
BRAE VILLAGE HOUSING PROJECT FOR THE 2007
PERMANENT SUPPORTIVE HOUSING PROGRAM"**

My Audit Division evaluated your response to the Report titled "Review of LAHD's Selection and Award to Bonnie Brae Village Housing Project (BBVHP) for the 2007 Permanent Supportive Housing Program." Your response indicates that LAHD agrees to implement the recommendations, and notes that the Department has implemented new processes, checklists and procedures to address the issues listed in the review report.

I accept your responses, with the exception of recommendation response number 5. Rather than offering a new procedure, you have restated existing LAHD competitive bidding policies allowing for design/build contracts, which you state is consistent with the conflict of interest code governing HOME activities noted in 24 CFR part 92.

HUD regulations do not offer blanket approval of construction contracts without competitive bidding. In cases where competitive bids are not received, HUD indicates that it could waive regulatory requirements of a competitive bidding, such as design/build, on a case-by-case basis, upon a written waiver request.

In addition, the BBVHP is an example of how your policy was not consistent with the approved loan agreement between LAHD and BBVP regarding covenants

Douglas Guthrie, General Manager
Los Angeles Housing Department
June 14, 2010
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addressing conflicts of interest stating that the borrower's (BBVP) shall have no interest, direct or indirect, in any contract or subcontract or the proceeds for work performed on the project. According to the City Attorney, the loan agreement was structured to reflect federal requirements.

LAHD must ensure that internal policies regarding selection and award of all projects complies with both the specific federal requirements, as well as with the spirit and intent of those requirements.

My Auditing staff may also follow up with your Department to ensure that actions detailed in your response are fully implemented. If you have any questions, you may contact Farid Saffar, Director of Auditing, at (213) 978-7392.

Sincerely,



WENDY GREUEL
City Controller

cc: Reverend Jeff Carr, Chief of Staff, Office of the Mayor
Jimmy Blackman, Deputy Chief of Staff, Office of the Mayor
Austin Beutner, Deputy Mayor, Mayor's Office
Matt Karatz, Managing Director, Mayor's Office
Miguel A. Santana, City Administrative Officer
June Lagmay, City Clerk
Gerry F. Miller, Chief Legislative Analyst
Independent City Auditors



OFFICE OF THE GENERAL MANAGER
Los Angeles Housing Department
LAHD

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tel 213.808.8808 | fax 213.808.8616
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Antonio R. Villaraigosa, Mayor
Douglas Guthrie, General Manager

June 7, 2010

Honorable Wendy J. Greuel
Los Angeles City Controller
Room 300, City Hall East
Los Angeles, CA 90012

Attention: Farid Saffar, Director of Auditing

Dear Honorable Greuel:

RE: RESPONSE TO AUDIT OF SELECTION AND AWARD TO BONNIE BRAE VILLAGE HOUSING PROJECT FOR THE 2007 PERMANENT SUPPORTIVE HOUSING PROGRAM

Thank you for your recent audit review entitled "Review of Los Angeles Housing Department's (LAHD) Selection and Award to Bonnie Brae Village Housing Project for the 2007 Permanent Supportive Housing Program." This audit was requested by LAHD senior management in order to have an outside and unbiased review of the decision making processes of the Affordable Housing Trust Fund. Specifically, to review whether appropriate fiscal controls and procedures had been followed with regard to the Bonnie Brae Village Partners residual receipts loan.

LAHD will work with the Mayor and the Controller's Office to implement the recommendations contained within this audit. A more detailed outline of the actions we have taken since receiving this audit are described in the attached Response to the Controller's Audit Work Plan.

In addition to the increased due diligence and controls LAHD has implemented, LAHD will work with the Housing Authority of the City of Los Angeles (HACLA) to improve the process for funding Permanent Supportive Housing Projects that rely upon joint funding by LAHD and HACLA.

Thank you for conducting your audit and providing us with the opportunity to respond. Should you have any questions, please contact Helmi Hisserich, Assistant General Manager at (213) 808-8662.

Sincerely,

DOUGLAS GUTHRIE
General Manager

Attachment

cc: Reverend Jeff Carr, Chief of Staff, Mayor's Office
Jimmy Blackman, Deputy Chief of Staff, Mayor's Office
Austin Beutner, Deputy Mayor, Mayor's Office
Matt Karatz, Managing Director, Mayor's Office
Miguel A. Santana, City Administrative Officer
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June Lagmay, City Clerk
Independent City Auditors

LOS ANGELES HOUSING DEPARTMENT

**Selection and Award to Bonnie Brae Village Housing Project for the
2007 Permanent Supportive Housing Program**

Response to Controller's Audit

FINDING	DESCRIPTION	RECOMMENDATION	RANKING	LAHD RESPONSE
1	<i>LAHD failed to perform thorough due diligence of a BBVP general partner and address inconsistencies between LAHD and State disclosure statements.</i>	<ol style="list-style-type: none"> Exercise due diligence by conducting a more thorough background investigation of developers and principal owners, especially in instances of inconsistent or questionable disclosure information, before making a LAHD loan approval recommendation. Disclose identified legal issues involving prospective applicants to the City Attorney, Mayor, Council and City Departments who have stakeholder interests. 	Urgent	<p>LAHD background investigation includes review of the developer's compliance with all LAHD operating units including: Systematic Code Enforcement, Rent Stabilization, Occupancy Monitoring, and Portfolio Management. The Portfolio Management review includes a check on property taxes, financial statements, insurance status, and current LAHD loan obligations. Developers are rejected from consideration for new funding unless they are in full compliance with all LAHD operating units.</p> <p>On 05/10/2010 LAHD initiated a new due diligence process to include:</p> <ul style="list-style-type: none"> Dunn & Bradstreet reports for each development team. A Lexus Nexus search of the development team and principals to determine any outstanding legal matters. <p>This due diligence process has been initiated on a temporary basis for the current applicants to 2010 Round II NoFA. After the NoFA review is complete, LAHD will evaluate the time, effort and cost for this increased due diligence. LAHD management will then evaluate the cost effectiveness of the process.</p> <p>As of May 15, 2010 LAHD will initiate a process to identify, review, and evaluate current or pending litigation of its applicants.</p> <p>The review will include analysis of the disclosure form, and a Lexus Nexus search of each development team to identify any undisclosed litigation.</p> <p>Failure to disclose material information will be grounds for denying the application for funding.</p> <p>LAHD will seek City Attorney review of all legal disclosures to determine what is and is not material. All material information will be disclosed to the Mayor, Council and any City Departments who have a stakeholder interest in the project.</p>
2	<i>LAHD submitted an application to the State of CA CDLAC requesting \$16.5 million in tax-exempt bond proceeds for the project, without performing an independent background review of one of the project's general partners.</i>	<ol style="list-style-type: none"> Prior to submitting an application for tax-exempt bond funding to the State, LAHD should verify the accuracy of information submitted, by conducting a thorough review and background investigation of developers and principal owners. 	Urgent	<p>As of May 15, 2010, prior to submitting an application for Tax Exempt Bond Funding, LAHD will conduct the review and background investigation identified in Response 1 above.</p>

FINDING	DESCRIPTION	RECOMMENDATION	RANKING	LAHD RESPONSE
3	<i>LAHD failed to require BBVP to secure an "Agreement to enter into Housing Assistance Payment (AHAP) Contract" with HACLA, prior to issuing a Notice to Proceed on construction.</i>	4. LAHD management should ensure that a "Notice to Proceed" is not issued to developers who fail to secure an Agreement to enter into Housing Assistance Payment (HAP) Contract with HACLA, when Section 8 vouchers are applicable.	Necessary	<p>LAHD has revised the pre construction checklist to include the requirement to enter into a Housing Assistance Payment ("HAP") contract with HACLA prior to issuing a NTP when Section 8 Vouchers are part of the funding source.</p> <p>A copy of the revised checklist is attached.</p>
4	<i>BBVP entered into an \$18.3 million construction contract with a general contractor owned by a BBVP general partner, in violation of LAHD's loan agreement covenant.</i>	5. LAHD management should establish a clear policy relating to the selection process of an entity having a dual role as both developer and general contractor, and ensure that policy is consistent with the Code of Federal Regulations.	Urgent	<p>The competitive bidding policy at LAHD policy allows for Developer Builder teams, who may be related entities to bid on construction as a design/build contract. This policy is clearly stated in both the AHTF NoFA Section 1.11.3 and the LAHD Major Projects Policies & Procedures Manual Section 3.4.1. This process is consistent with the conflict of interest code governing HOME activities 24 CFR Part 92.</p> <p>LAHD management believes the advantages of allowing developer / general contractor teams to submit a design build construction estimate outweigh the disadvantages of potential abuse. However, LAHD recognizes the importance of ensuring construction costs between related parties do not result in a misuse of taxpayer funds.</p> <p>LAHD's construction services unit performs an independent cost review prior to each loan closing and will continue to do this on all future loans.</p> <p>In addition, LAHD management is evaluating the use of a guaranteed maximum (G-Max) construction contract rather than its current policy of a fixed price contract. The current stipulated sum contract used at LAHD sets the amount of the construction at the beginning of the transaction. Changing to a cost plus guaranteed maximum price contract (G-Max) would ensure any cost savings in the project are realized by the LAHD, rather than returned to the developer.</p> <p>The G-max contract may be implemented for all new projects awarded funding through the 2010 Round II NoFA. As of May 15, 2010 LAHD management has a new boiler plate G-max contract under review.</p>
5	<i>LAHD's "gap" financing loan award should have been reduced before entering into a loan agreement based on the reduction of BBVP's cost estimate.</i>	6. LAHD management should ensure that available City funds are appropriately allocated, and projects are not overfunded with "gap financing" proceeds, as a result of value engineering or any other factors affecting project costs.	Necessary	<p>See above change to a G-Max contract.</p> <p>All increases to construction commitments will be reviewed and signed off by the General Manager or Assistant General Manager.</p>
6	<i>BBVP submitted requests to LAHD for reimbursement of payments in violation of the loan agreement.</i>	NONE	N/A	N/A

FINDING	DESCRIPTION	RECOMMENDATION	RANKING	LAHD RESPONSE
7	<i>BBVP substituted a qualified tenant relocation contractor for an inexperienced subcontractor who failed to abide by relocation guidelines.</i>	NONE	N/A	N/A
8	<i>LAHD did not monitor or have an accounting of the uses of tax exempt bond funds for the project.</i>	7. LAHD management should review and maintain an accounting of all developer reimbursement draw requests from all project sources, and monitor to ensure that project disbursements are made in accordance with the approved project budget.	Necessary	<p>LAHD currently reviews and approves all disbursements of bond proceeds after verifying that work is completed, soft costs are eligible and there is no duplication of payments for items funded through the LAHD loan.</p> <p>As of June 15, 2010 the following steps will be taken to ensure this process is carried out effectively.</p> <ul style="list-style-type: none"> • LAHD will be added to the distribution list for Trustee Statements. • Line item detail budget worksheets will be required for all soft cost draw requests.
9	<i>LAHD allowed BBVP to incorporate increases in cash reserves from the originally approved budget adversely impacting repayments on the LAHD loan.</i>	8. LAHD management should ensure that the City's financial interests are protected before allowing modifications to originally approved financing commitments.	Urgent	<p>Standard operating and replacement reserves are capped by LAHD based on industry standards. However lenders and investors require projects involving Section 8 operating subsidies to maintain additional accounts known as transition reserves. Section 8 contracts have a 10-15 year term but are subject to annual appropriations from HUD.</p> <p>These funds are required to be available in the event that the Section 8 contract is not renewed at some time in the future. Without the operating subsidy the formerly homeless tenants could not afford to pay the rent and the building would need to be converted into a low income housing development without rental subsidies. The existing tenants would need to be replaced, and the project revenues would decrease.</p> <p>The exact reserve amount is set prior to permanent loan closing based on the most recent rent and expense projections which change over time. The reserve is sized to pay the expenses and debt service during the turn over period of at least two years. Reserve requirements exceeding this amount require approval of the Assistant General Manager.</p> <p>This process will be included in the LAHD policies and procedures manual as of June 15, 2010.</p>
10	<i>Some of the changes to the ownership and organizational structure of BBVP may be consistent with industry practice; however, legal implications resulting from the changes are unknown.</i>	NONE	N/A	N/A

LOS ANGELES HOUSING DEPARTMENT

Construction Services Unit

PRE-CONSTRUCTION PACKAGE CHECKLIST

**Please check-off and provide the following items in order to obtain an
Authorization to Issue Notice to Proceed:**

1. Contractor Information Form.....
 - a. Copy of Contractor License.....
2. 3 Bids from General Contractors or Subcontractors.....
3. Construction Contract Draft with Schedule of Values on AIA Format.....
 - a. Signed Construction Contract.....
4. Schedules: Construction Work Schedule and Payment Schedule.....
5. Permits.....
6. Insurance:
 - a. General Liability Certificate.....
 - b. Workers' Compensation Certificate
7. Other Submittals (if applicable):
 - a. Updated Soils Report.....
 - b. Plans and Specifications and Plan check submittal number.....
 - c. Project Needs Assessment Report.....
 - d. Detailed Scope of Work.....
 - e. Lead based Paint and Asbestos Reports.....
8. Performance and Payment Bond.....
9. Authorization to Issue the Notice to Proceed

FOR LAHD INTERNAL USE ONLY

1. Executed *Agreement to Enter into a Housing Assistance Payments Contract (AHAP)* with HACLA (applicable to all PSHP projects).....
2. Federal Debarment Certification
3. Approval from Prevailing Wage Compliance Unit
4. Pre-Construction Conference.....
5. Environmental Unit Clearance.....
6. Builder's Risk Insurance
7. Executed Intercreditor Agreement
8. Executed Loan Agreement
9. Owner/Contractor Notice to Proceed