



The Commonwealth of Massachusetts
Office of the Inspector General

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October 23, 2007

Tina Brooks, Undersecretary
Department of Housing and Community Development
100 Cambridge Street - Suite 300
Boston, MA 02114

Dear Undersecretary Brooks,

As shared with you at our meeting yesterday, recent reviews by my Office of housing developments created under Chapter 40B have uncovered numerous abuses by developers. It is essential that strong oversight and control be instituted through the central administration of Chapter 40B. Without adequate oversight and control not only are municipalities put at risk but the integrity of the Chapter 40B program is compromised and the overall credibility of affordable housing initiatives in the Commonwealth is adversely impacted.

A major source of the problem is the fact that through previous administrations, DHCD had abdicated its vital oversight role to the subsidizing agencies. These banks or subsidizing agencies have an inherent bias. The business relationship between the bank and the developer stands in the way of effective, meaningful, and independent or arms-length cost monitoring efforts. This lender/customer relationship results in behaviors which run counter to the interests of the municipalities and is evidenced again in the recently published MassHousing cost certification guidelines. Due to these inherent biases it is imperative that DHCD assume a strong central leadership role in the Chapter 40B cost oversight process.

DHCD needs to promulgate regulations addressing Chapter 40B oversight and control. Specifically, cost certification procedures should be issued by DHCD through regulations and not by subsidizing agencies through guidelines. Abdicating this role to subsidizing agencies leads to different rules being applied and, ultimately, a lack of oversight and an environment prone to abuse.

Highlighted below are some of the fundamental changes that should quickly be implemented in order to help ensure a fair, open and transparent oversight process:

Prequalification of Certified Public Accountants, Appraisers & Monitoring Agents:

DHCD should create and maintain lists of certified public accountants, appraisers and monitoring agents who are approved to participate in the Chapter 40B process. This prequalification should be done by DHCD and not the subsidizing agencies or developers.

Selection of Appraisers, Certified Public Accountants & Monitoring Agents: The appraiser used to determine the land acquisition value should be chosen by the municipality from the pre-qualified list of appraisers created by DHCD. It should not be an appraiser chosen by the developer from a list created by the subsidizing agency. Similarly the certified public accountant and the monitoring agent should also be chosen by the municipality from pre-qualified lists created and maintained by DHCD. The recently published MassHousing cost certification guidelines perpetuate an environment susceptible to developer abuse. These guidelines block the municipalities from any effective role in the process and neutralize legitimate efforts on the part of the municipalities in protecting their financial interests. Maintaining an oversight process which relies on developer selected certified public accountants and appraisers does little to eradicate the fraud and abuse in the current system.

Definitions: The regulations should address definitions for the various allowable development costs and for development revenue. Reasonable return or limited dividend should also be articulated in the regulations.

Submissions under Pains of Perjury: In addition to the cost certification report, all Chapter 40B applications (such as project eligibility/site approval and comprehensive permit, etc.) should be submitted under pain and penalty of perjury. The recent MassHousing guidelines address this requirement for cost certifications but this should be extended to the other submissions.

Sanctions for failure to submit or late submissions: Regulations should address sanctions against developers who fail to submit a cost certification on a timely basis. Penalties and interest should accrue. The regulations should require developers to post adequate forms of guaranty which will help ensure timely project completion and cost certification compliance. This is not addressed through the MassHousing guidelines.

Land Acquisition Costs: As mentioned above the municipality should select a DHCD qualified appraiser to determine the allowable land value. The appraiser should follow the land valuation rules promulgated through DHCD regulations. The November 2005 MHP guidelines provide a clear and basic land valuation rule: "The value should relate directly to the as-is value of the site under current zoning and should not be artificially inflated as a result of the extra value provided by a comprehensive permit or a non-arm's length conveyance between related parties." The MassHousing cost certification

guidelines have altered the previously endorsed MHP guidelines by inserting the following language: "The appraisal commissioned by the Project Administrator may, in accordance with USPAP, take into account the probability of obtaining a variance, special permit or other zoning relief, but it must exclude any value relating to the possible issuance of a comprehensive permit under Chapter 40B". This underscores the need for clear central regulatory guidance through DHCD as opposed to different perspectives from the various banking or subsidizing organizations.

Attestation Standards: The new MassHousing cost certification guidelines reduce the level of oversight by inserting an "examination" as opposed to the previously established "audit" requirement. This Office urges that the audit requirement be reestablished for all projects and that consideration is given that these audits are done under the more rigorous Government Auditing Standards (GAS) versus the American Institute of Certified Public Accountants (AICPA) standards. As an example note that under AICPA an auditor need only detect noncompliance relating to illegal acts, whereas under GAS an auditor would also have to detect violations of provisions of contracts and grant agreements as well. The most important element to ensure a fair, open and transparent oversight process is acknowledging the interests of the municipalities and allowing the municipalities to select the necessary certified public accountants, appraisers and monitoring agents. Independent audits and appraisals which eliminate the current conflicts of interest intrinsic with developer selection of auditors and appraisers are essential.

As stated before, there is an inherent bias on the part of subsidizing agencies to support their clients (developers) at the expense of municipalities. In the past DHCD has been complicit, albeit unwittingly, in enabling developers to cheat the system. Recently, when DHCD (Jane Wallis Gumble) and the subsidizing agencies (MassHousing) were informed of the pervasive developer abuse in the system, the reaction from DHCD/MassHousing was to "circle the wagons". Rather than taking decisive measures to eradicate the fraud and abuse in the system, the reaction from the banks and DHCD was to put up barriers to external oversight. DHCD issued additional guidance and MassHousing implemented changes to their regulatory agreements that effectively blocked involvement in the oversight process by municipalities. MassHousing incorporated an acknowledgement statement in their regulatory agreements that members of local zoning boards of appeals are required to sign. This acknowledgement states that the limited dividend requirement is to be determined solely by the project administrator and that the regulatory agreement will control over any conflicts with the comprehensive permit. The new MassHousing cost certification guidelines are an extension of this misplaced reaction. These new guidelines continue to keep the municipalities and effective oversight efforts at bay.

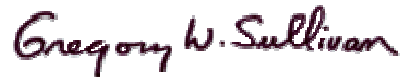
The current cost certification process and the new MassHousing guidelines do not provide adequate protections for municipalities. The MassHousing guidelines do little to curb the abuses my office has uncovered. These guidelines allow municipalities very little involvement in the process. Municipalities are allowed the very limited time of

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thirty days to evaluate the cost certification. As the administration has publicly stated local governments face very tight fiscal restraints. It will be difficult for them to divert staff from other duties to review the cost certification in such a limited timeframe. Also, municipalities are not given access to source documents which will make it very difficult to do a proper evaluation of the cost certification. The regulatory agreement used by MassHousing also distances the municipality from the process. A piecemeal process administered by each individual subsidizing agency will not solve the legitimate problems that currently exist in 40B developments. To end the abuse DHCD needs to put forth strong regulations that the subsidizing agencies must follow and which fully engage the municipalities.

As you evaluate DHCD's 40B regulations, I look forward to the opportunity to have more in-depth discussions regarding the safeguards DHCD can put into place to alleviate some of the abuses currently being perpetrated under 40B. If I can be of any further assistance, please do not hesitate to call me.

Sincerely,

A handwritten signature in dark ink that reads "Gregory W. Sullivan". The signature is written in a cursive, slightly slanted style.

Gregory W. Sullivan
Inspector General