



Commonwealth of Massachusetts
Office of the State Auditor
Suzanne M. Bump

Making government work better

Official Audit Report – Issued August 17, 2011

Chelmsford Housing Authority

For the period January 1, 2008 through June 30, 2010



TABLE OF CONTENTS/EXECUTIVE SUMMARY

INTRODUCTION

1

In accordance with Chapter 11, Section 12, of the Massachusetts General Laws, the Office of the State Auditor has conducted an audit of certain activities of the Chelmsford Housing Authority for the period January 1, 2008 through June 30, 2010. The objectives of our audit were to review and analyze the Authority's management controls and practices over certain areas and functions for the purpose of determining their adequacy, and review its compliance with laws, rules, and regulations. In addition, we reviewed the Authority's progress in addressing the conditions noted in our prior audit report (No. 2008-0630-3A).

Based on our review, we have concluded that, except for the issues addressed in the Audit Results section of this report, for the period January 1, 2008 through June 30, 2010, the Authority maintained adequate management controls and complied with applicable laws, rules, and regulations for the areas tested.

AUDIT RESULTS

3

1. PRIOR AUDIT RESULTS PARTIALLY RESOLVED

3

Our prior audit of the Authority (No. 2008-0630-3A), which covered the period July 1, 2005 to December 31, 2007, noted that improvements were needed in the areas of (a) compliance with Chapter II of the State Sanitary Code and (b) Department of Housing and Community Development (DHCD) funding of modernization initiatives. Our follow-up review indicated that the Authority has partially resolved these issues, as follows:

a. Compliance with State Sanitary Code

3

Our prior audit noted that the Authority had addressed many of the instances of noncompliance with Chapter II of the State Sanitary Code. However, two issues were not addressed because DHCD denied the Authority's funding requests for siding at the 667-5 development and kitchen renovations at the 667-1 development.

Our follow-up review indicated that the Authority has been repairing the siding and renovating the kitchens as needed. Moreover, the Authority's Executive Director noted that DHCD will be providing funding for repairs over the next three years through its formula funding program.

b. Modernization Initiatives

3

Previously, DHCD funded its capital improvement projects through individual modernization awards. In June 2010, DHCD initiated a formula funding program to ensure that capital funds awarded to state-aided public housing authorities are distributed in an equitable and predictable manner. Beginning in fiscal year 2012, local housing authorities will receive a multi-year award of funds that can be used to plan for and implement capital fund improvements.

Our prior audit noted that the Authority received modernization funding to repair issues at its developments; however, two issues were not addressed: a drainage issue at the

667-1 development and, as noted above, siding repairs at the 667-5 development. Also, our prior audit noted that although the Authority indicated that it had requested DHCD's permission to sell the six condominiums at its 667-4 development due to the annual costs to maintain the condominiums, DHCD had refused the request.

Our follow-up review indicated that the drainage repairs are no longer necessary because a construction project at the 667-1 development has been canceled and that the Authority has been repairing the siding as needed. In addition, the Executive Director stated that the sale of the condominiums is under review and that, if the condominiums are sold, the funds will be utilized for new housing units.

2. MEDICARE TAX WITHHELD INCORRECTLY **4**

Our review of the Authority's payroll records disclosed that the Authority was incorrectly withholding Medicare taxes from its maintenance worker's salary. We determined that during calendar years 2008 through 2010, the Authority incorrectly withheld \$1,407 in Medicare taxes from this employee and paid the matching portion of the tax. We brought the matter to the attention of the Executive Director, and the Authority is correcting its tax filings for these three years.

3. IMPROVEMENTS NEEDED IN CALCULATING ASSET DEPRECIATION **5**

Our review revealed that errors were made in the Authority's calculation of the accumulated depreciation of its assets, which resulted in an overstatement of \$909,476 in the Authority's accumulated depreciation financial statement balance for its 400-1 project. The error occurred in part because the Authority in two instances did not use the correct date for when the assets were placed in service and a building asset was expensed prematurely rather than allocated over its estimated useful life of 40 years.

4. IMPROVEMENTS NEEDED IN INVENTORY CONTROL **7**

We found that the Authority did not maintain a complete, up-to-date inventory listing of its furniture and equipment. The Executive Director stated that although the Authority had reviewed the inventory list as required by DCHD, it did not update the list. At the close of our audit, the Executive Director indicated that the Authority had updated the state fixed-asset list and the Board of Directors was approving the disposition/destruction of items that should have been removed.

INTRODUCTION

Audit Scope, Objectives, and Methodology

In accordance with Chapter 11, Section 12, of the Massachusetts General Laws, we have conducted an audit of certain activities of the Chelmsford Housing Authority for the period January 1, 2008 through June 30, 2010. The objectives of our audit were to determine the Authority's compliance with applicable laws, rules, and regulations and to review and analyze its management controls and practices over the following areas and functions for the purpose of determining their adequacy: (1) tenant selection; (2) preparation and reoccupation of vacant units; (3) rent determinations; (4) collectability of accounts receivables; (5) site inspections; (6) payroll, travel, and fringe benefits; (7) disbursements; (8) inventory controls over property and equipment; (9) contract procurement; (10) cash management and investment practices; (11) Department of Housing and Community Development (DHCD)-approved budgets versus actual expenditures; (12) level of need for operating subsidies and operating reserves; (13) administration of development and modernization funds to determine, among other items, the existence of excess funds; and (14) the Massachusetts Rental Voucher Program. We also conducted a follow-up review of the Authority's progress in addressing the issues noted in our prior audit report (No. 2008-0630-3A).

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.

To achieve our audit objectives, we reviewed the following:

- Tenant-selection procedures to verify that tenants were selected in accordance with DHCD regulations.
- Vacancy records to determine whether the Authority adhered to DHCD procedures for preparing and filling vacant housing units.
- Annual rent-determination procedures to verify that rents were calculated properly and in accordance with DHCD regulations.
- Accounts receivable procedures to ensure that rent collections were timely and that uncollectible tenants' accounts receivable balances were written off properly.

- Site-inspection procedures and records to verify compliance with DHCD inspection requirements and that selected housing units were in safe and sanitary condition and to determine whether the Authority has in place an updated official written property maintenance plan for its managed properties.
- Procedures for making payments for payroll, travel, and fringe benefits to verify compliance with established rules and regulations.
- Authority expenditures to determine whether they were reasonable, allowable, and applicable to the Authority's operations and were adequately documented and properly authorized in accordance with established criteria.
- Property and equipment inventory-control procedures to determine whether the Authority properly protected and maintained its resources in compliance with DHCD requirements.
- Contract procurement procedures and records to verify compliance with public bidding laws and DHCD requirements for awarding contracts.
- Cash management and investment policies and practices to verify that the Authority maximized its interest income and that its deposits were fully insured.
- DHCD-approved operating budgets for the fiscal year in comparison with actual expenditures to determine whether line-item and total amounts by housing program were within budgetary limits and whether required fiscal reports were submitted to DHCD in a complete, accurate, and timely manner.
- Operating reserve accounts to verify that the Authority's reserves fell within DHCD provisions for maximum and minimum allowable amounts and to verify the level of need for operating subsidies to determine whether the amount earned was consistent with the amount received from DHCD.
- Development and modernization awards to verify that contracts were awarded properly and funds were received and disbursed in accordance with the contracts, and to determine the existence of any excess funds.
- Procedures for making payments to landlords under the Massachusetts Rental Voucher Program to verify compliance with the contract provisions and that rental charges by landlords were consistent with established rules and regulations.
- The Authority's progress in addressing the issues noted in our prior audit report (No. 2008-0630-3A).

Based on our review, we have concluded that, except for the issues addressed in the Audit Results section of this report, for the period January 1, 2008 through June 30, 2010, the Authority maintained adequate management controls and complied with applicable laws, rules, and regulations for the areas tested.

AUDIT RESULTS

1. PRIOR AUDIT RESULTS PARTIALLY RESOLVED

Our prior audit report of the Chelmsford Housing Authority (No. 2008-0630-3A), which covered the period July 1, 2005 to December 31, 2007, noted that improvements were needed in the areas of (a) compliance with Chapter II of the State Sanitary Code and (b) Department of Housing and Community Development (DHCD) funding of modernization initiatives. Our follow-up review indicated that the Authority has partially resolved these issues, as follows:

a. Compliance with State Sanitary Code

Our prior audit noted that the Authority had addressed many of the instances of noncompliance with Chapter II of the State Sanitary Code. However, two issues were not addressed because DHCD denied the Authority's funding requests for siding at the 667-5 development and kitchen renovations at the 667-1 development. During our follow-up review the Executive Director indicated that the Authority has been repairing the siding and renovating the kitchens as needed. Moreover, the Authority's Executive Director noted that DHCD will be providing funding for repairs over the next three years through its formula funding program.

b. Modernization Initiatives

Previously, DHCD funded its capital improvement projects through individual modernization awards. In June 2010, DHCD initiated a formula funding program to ensure that capital funds awarded to state-aided public housing authorities are distributed in an equitable and predictable manner. Beginning in fiscal year 2012, Authorities will receive a multi-year award of funds that can be used to plan for and implement capital fund improvements.

Our prior audit noted that the Authority received modernization funding to repair issues at its developments; however, two issues were not addressed: a drainage issue at its 667-1 development and, as noted above, siding repairs at the 667-5 development. Our follow-up review indicated that the drainage repairs are no longer necessary because a construction project at the 667-1 project has been canceled and the Authority has been repairing the siding as needed.

Also, the Authority indicated that it had requested DHCD's permission to sell the six condominiums at its 667-4 development due to the annual costs to maintain the condominiums; however, DHCD had refused the request. The Executive Director stated that the sale of the condominiums is under review and if the condominiums are sold the funds will be utilized for new housing units.

Recommendation

The Authority should consider using funds from the formula funding program to finish renovating the kitchens and remedy the siding issue. In addition, the Authority should continue to work with DHCD on the sale of the condominiums.

Auditee's Response

The CHA (Chelmsford Housing Authority) has received notification from DHCD regarding their formula funding allocation for the next three years. Based upon the Capital Improvement System (CIS) database provided through DHCD, there are higher priorities that have been identified that the CHA should consider utilizing the limited amount of formula funding that is being provided. The CHA is committed to incorporating the items identified in the audit into our overall plan.

2. MEDICARE TAX WITHHELD INCORRECTLY

Our review of the Authority's payroll records disclosed that the Authority was incorrectly withholding Medicare taxes from its maintenance worker's salary. The Maintenance Supervisor was hired in 1982 and, in accordance with Internal Revenue Service (IRS) regulations, was not subject to having Medicare taxes withheld from his pay. We determined that the Authority incorrectly withheld \$1,407 in Medicare taxes from this employee and paid the matching portion of the tax for calendar 2008, 2009, and 2010.

The Authority indicated that it incorrectly withheld Medicare taxes because it was unaware of the IRS exemption. Because the maintenance employee started and continued his employment with the Authority and is a member of a public retirement system, he and the Authority were exempt from having to pay Medicare taxes. Specifically, IRS Publication 963 states, in part:

Services performed after March 31, 1986, by an employee who was hired by a state or political subdivision employer before April 1, 1986, are exempt from mandatory Medicare tax if the employee is a member of a public retirement system and meets all of the following requirements:

- *The employee was performing regular and substantial services for remuneration for the state or political subdivision employer before April 1, 1986,*
- *The employee was a bona fide employee of that employer on March 31, 1986,*
- *The employment relationship with that employer was not entered into for purposes of avoiding the Medicare taxes, and*
- *The employment relationship with that employer has been continuous since March 31, 1986.*

We found that the maintenance worker met each of these conditions and therefore should not have had Medicare taxes deducted from his paycheck.

We brought the matter to the attention of the Executive Director, and the Authority is correcting its tax filings for calendar 2008, 2009 and 2010. The Authority should take action to recover the overpayments and provide a refund to the employee, who retired on June 30, 2010.

Recommendation

The Authority should file for a reimbursement of the taxes paid on behalf of the employee and the matching portion paid by the Authority. Once reimbursement is received, the Authority should reimburse the maintenance worker for the overpayment of the taxes.

Auditee's Response

The CHA has completed the requests for reimbursement and is awaiting the refund. In addition, we have notified the former employee of this situation. The only outstanding matter is to provide the reimbursement to the employee.

3. IMPROVEMENTS NEEDED IN CALCULATING ASSET DEPRECIATION

Our review revealed that errors were made in the Authority's calculation of the accumulated depreciation of its assets, which resulted in an overstatement of \$909,476 in the Authority's accumulated depreciation financial statement balance for its 400-1 project. Section 19 of DHCD's Accounting Manual describes depreciation as follows:

The systematic allocation of the depreciable amount of an asset over its useful life. Depreciable amount is the cost of an asset, or other amount substituted for cost in the financial statements, less its residual value. Useful life is either: a) the period of time over which an asset is expected to be used by the enterprise or, b) the number of production or similar units expected to be obtained from the asset by the enterprise. Cost is amount of cash or cash equivalents paid or the fair value of other consideration given to acquire an asset at the time of its acquisition or construction. Residual value is the net amount, which the enterprise expects to obtain for an asset at the end of its

useful life after deducting the expected cost of disposal. When depreciating fixed assets, the Local Housing Authority should establish useful lives for these assets that reflect reasonable estimates of the assets' lives.

The error occurred in part because the Authority's fee accountant in two instances did not use the correct date for when the assets were placed in service. We found that the Authority's fee accountant calculated the accumulated depreciation for the 667-5 program using a starting date of 1981 when the project was not put into service until 1990, and for the 705 program the fee accountant used a starting date of 1985 rather than 1990. Also, in calculating the 667-4 program's depreciation, the fee accountant expensed the item prematurely rather than allocating the building asset over its estimated useful life of 40 years. Although these errors are reflected in the financial statements for fiscal years 2008 and 2009, we summarized the variances as of June 30, 2010 in the table below:

<u>Program</u>	Authority's Accumulated Depreciation Balance Fiscal Year <u>2010</u>	Actual Accumulated Depreciation Balance Fiscal Year <u>2010</u>	<u>Variance</u>
667-4	\$ 167,320	\$ 121,307	\$ 46,013
667-5	2,334,895	1,610,272	724,623
705	<u>694,200</u>	<u>555,360</u>	<u>138,840</u>
	<u>\$ 3,196,415</u>	<u>\$ 2,286,939</u>	<u>\$ 909,476</u>

Because the accumulated depreciation for the Authority's assets was not properly allocated, the Authority's financial statements do not properly reflect the correct asset value as of June 30, 2010.

Recommendation

The Authority should ensure that all assets are depreciated correctly, make the necessary adjustments to its accounting records, and resubmit corrected financial statements to the appropriate agencies.

Auditee's Response

The Fee Accountant indicated that there was a transcription error and that it would be corrected this fiscal year.

4. IMPROVEMENTS NEEDED IN INVENTORY CONTROL

We found that the Authority did not maintain a complete, up-to-date inventory listing of its furniture and equipment. DHCD's Accounting Manual for State-Aided Housing Programs, Section 15, states, in part:

A formal system for the inventory of furniture and equipment [shall] be established by program by all LHAs [Local Housing Authorities]. The inventory will be composed of two separate parts; a capital inventory which will include all furniture and equipment costing \$5,000 or more which will be capitalized and depreciated and a non capital/control inventory for all items expensed at purchase but costing \$1,000 or more (refrigerators and stoves are to included regardless of price).

In addition, DHCD has outlined the following inventory procedures:

Establish furniture and Equipment Record Cards or use an automated system. Tag all inventory with an inventory tag with assigned asset number. Take an inventory once a year.

We reviewed the Authority's inventory list for accuracy and randomly selected 10 items which we were able to locate at the Authority. However, we reviewed the inventory list with the Executive Director and found three items--a copier, computer equipment and a 1994 pickup truck--that had been disposed of by the Authority were still on the inventory list. Also, we noted a telephone system with a cost of \$5,472 which was listed on the inventory list but was not listed on the Authority's depreciation schedule. All items which have a value of \$5,000 or more should be listed on the Authority's depreciation list. Finally, we found a snow blower that was listed on the Authority's depreciation list that was not on the inventory list. The Executive Director stated that although the Authority had reviewed the inventory list as required by DHCD, it did not update the list. At the close of our audit, the Executive Director indicated that the Authority had updated the state fixed asset list and the Board of Directors was approving the disposition/destruction of items that should have been removed. An inventory list that is not updated and verified annually provides inadequate assurance that the Authority's assets are adequately safeguarded against possible loss, theft, or misuse.

Recommendation

The Authority should continue to review all of its assets and update its inventory list annually to ensure that all assets are adequately accounted for in accordance with DHCD's inventory policy.

Auditee's Response

The CHA . . . had disposed of the items as required by our Disposition Policy. The CHA Board reviewed the corrected inventory list which addressed all concerns raised by the Auditors. This has been fully resolved.