

Audit Report

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**Department of Housing and Community Development**

**Office of the Secretary  
Division of Finance and Administration  
Division of Information Technology**

February 2009

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**OFFICE OF LEGISLATIVE AUDITS  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY**

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Karl S. Aro  
Executive Director

DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Bruce A. Myers, CPA  
Legislative Auditor

February 19, 2009

Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee  
Senator Verna L. Jones, Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

Ladies and Gentlemen:

We have audited the Office of the Secretary, the Division of Finance and Administration, and the Division of Information Technology within the Department of Housing and Community Development (DHCD) for the period beginning July 1, 2005 and ending June 30, 2008. These units perform administrative and oversight functions to assist DHCD in achieving its goals of strengthening communities and providing affordable housing for people of limited income.

Our audit disclosed that DHCD did not ensure that all funds due to the Maryland Affordable Housing Trust were received and that all grantee reports were obtained. In addition, although DHCD's former Division of Historical and Cultural Programs was transferred to the Maryland Department of Planning effective October 1, 2005, the related property and equipment records had not been transferred to MDP.

Our audit also disclosed control and record keeping deficiencies related to equipment and year-end closing transactions.

DHCD's response to this audit is included as an appendix to this report. We wish to acknowledge the cooperation extended to us during the course of this audit by DHCD.

Respectfully submitted,

Bruce A. Myers, CPA  
Legislative Auditor



# Table of Contents

<b>Background Information</b>	4
Agency Responsibilities	4
Status of Findings From Preceding Audit Report	4
<b>Findings and Recommendations</b>	5
<b>Maryland Affordable Housing Trust</b>	
*    Finding 1 – DHCD Did Not Ensure That All Funds Due to the Trust Were Received and That Grantee Reports Were Obtained	5
<b>Property</b>	
Finding 2 – Property and Equipment Records Have Not Been Properly Transferred to the Maryland Department of Planning	7
Finding 3 – DHCD Had Not Established Adequate Accountability and Control Over Equipment	8
<b>Year-End Closing Transactions</b>	
Finding 4 – DHCD Recorded Federal Fund Accrued Revenues for Which Funding May Not Be Available	9
<b>Audit Scope, Objectives, and Methodology</b>	10
<b>Agency Response</b>	Appendix

\* Denotes item repeated in full or part from preceding audit report

## **Background Information**

### **Agency Responsibilities**

The Department of Housing and Community Development (DHCD) provides services to strengthen communities and provides affordable housing for people of limited income. The mission of DHCD is to work with partners to finance housing opportunities and revitalize places for Maryland citizens to live, work, and prosper. To deliver these services, the Department is organized into six units. This audit report includes the operations of the following three units:

Office of the Secretary  
Division of Finance and Administration  
Division of Information Technology

The remaining units of the Department (Division of Credit Assurance, Division of Development Finance, and Division of Neighborhood Revitalization) are included within the scope of, and reported upon in, a separate audit. According to the State's accounting records, during fiscal year 2008, total DHCD expenditures were approximately \$285.8 million, of which \$16.4 million related to the units audited.

### **Status of Findings From Preceding Audit Report**

Our audit included a review to determine the status of the seven findings contained in our preceding audit report dated April 12, 2006. We determined that DHCD had satisfactorily resolved six of these findings. The remaining finding is repeated in this report.

## Findings and Recommendations

### Maryland Affordable Housing Trust

#### **Finding 1**

**The Department of Housing and Community Development (DHCD) did not ensure that all funds due to the Maryland Affordable Housing Trust (MAHT) were received and that all grantee reports were obtained.**

#### **Analysis**

DHCD did not adequately ensure that all funds due to the MAHT were received. Additionally, required MAHT grantee reports were not always obtained. MAHT is a charitable public corporation administered by DHCD to promote affordable housing in the State. It acquires funds through interest earned on title insurance companies' escrow accounts and awards grants to eligible applicants (such as nonprofit organizations and local government agencies) for activities, such as acquisition, construction, rehabilitation or preservation of affordable housing, and operating expenses of housing developments that promote affordable housing. According to DHCD records for fiscal year 2008, escrow income received totaled approximately \$3.1 million and grant awards totaled \$3.7 million. Specifically, we noted the following conditions:

- DHCD did not adequately pursue title companies that failed to submit required annual reports. Since these reports are used to identify funds to be remitted to MAHT, DHCD lacked assurance that all escrow funds due to MAHT were received. Specifically, State regulations require that financial institutions forward, at least quarterly, these escrow funds to MAHT and that each title company file an annual report of the escrow funds due to MAHT by March 31<sup>st</sup> for the immediately preceding calendar year. According to DHCD's computerized records of annual reports, which we tested and found to be reliable, as of June 2008, 890 out of 1,539 title companies (58 percent) had not submitted annual reports for calendar year 2007; 746 out of 1,464 title companies (51 percent) had not submitted annual reports for calendar year 2006; and 525 out of 1,290 title companies (41 percent) had not submitted annual reports for calendar year 2005. A similar condition was commented upon in our prior audit report.

To address this issue, effective December 2006, the Maryland Insurance Administration (MIA) agreed to assist DHCD in monitoring and enforcement of reporting compliance as part of its oversight responsibilities over title companies. We were advised that MIA requested MAHT to cease follow up on calendar year 2005 accounts, and to focus on calendar year 2006 and 2007

accounts. However, as of September 2008, DHCD had only referred 150 title companies to MIA for assistance, due to MIA's workload and available resources. According to DHCD's records, as of September 2008, 1,202 additional title companies from 2007 and 2006 could have been referred to MIA.

Furthermore, as of September 2008, for the aforementioned annual reports that were obtained, reconciliations of funds to be remitted as reported by the title companies to funds actually received had not been performed for calendar year 2007. We were advised by DHCD management that the reconciliations were not performed because a new data base system is being implemented to monitor the title companies.

- DHCD did not require that the annual escrow reports from the title companies contain information on the types and amounts of service charges on escrow accounts. Consequently, DHCD could not verify the appropriateness of reported service charges. State regulations specify that only reasonable and customary charges for commercial accounts may be deducted; such charges do not include bank charges for bad checks, overdrafts, certified checks, and account reconciliations. A similar condition was commented upon in our prior audit report.
- Our test of 10 MAHT grant awards totaling \$947,500, for fiscal years 2007 and 2008, disclosed that grantees did not always submit required reports, which would allow DHCD to monitor grantees to ensure funds were being spent in accordance with the related grant agreements. Specifically, 8 of the 10 grantees failed to submit all quarterly progress reports as required by the related grant agreements. In this regard, we noted that the 8 recipients, who received grant awards totaling \$782,500, had only submitted 2 of the 35 reports that should have been submitted for the quarters during the period from March 31, 2007 to June 30, 2008. Additionally, although 4 of the grantees tested were required to submit an annual report of household income in order to verify that the residents met income thresholds, these reports were not submitted. Finally, for 5 grantees, final grant reports were required; however, 4 of these 5 grantees did not submit the final reports.

### **Recommendation 1**

#### **We recommend that DHCD**

- a. establish procedures for following up with title companies to ensure that annual reports are submitted, with all required supporting documentation, by the March 31<sup>st</sup> deadline as required by State regulations (repeat);**

- b. in conjunction with MIA, eliminate the backlog of title companies that have not submitted required annual reports;**
- c. perform reconciliations of the funds to be remitted by the title companies as reported in annual reports received with the funds actually received in a timely manner; and**
- d. ensure that MAHT grantees submit reports as required and use the reports to ensure funds are expended in accordance with related grant requirements.**

## **Property**

### **Finding 2**

**Records for property and equipment totaling approximately \$25.7 million had not been transferred to the Maryland Department of Planning (MDP).**

### **Analysis**

As of October 2008, the records for property (such as land and buildings) and equipment with a book value of approximately \$24.7 million and \$1 million, respectively, had not been transferred to MDP in accordance with the October 1, 2005 transfer of DHCD's former Division of Historical and Cultural Programs to MDP. Additionally, in conjunction with the Division's transfer to MDP, neither DHCD nor MDP established a process to ensure that all Division property and equipment was properly accounted for. In this regard, although DHCD's records indicate that equipment totaling approximately \$1 million should have been transferred to MDP, a subsequent physical inventory performed by MDP in October 2007 identified Division equipment on hand totaling only \$741,000. As of October 2008, neither agency could account for the discrepancy. In addition, the required Department of General Services' (DGS) approval to transfer this equipment to MDP had not been obtained.

The DGS *Inventory Control Manual* specifies the procedures for investigating, reporting to DGS, and removing records for missing items. The *Manual* also specifies the procedures for transferring capital items, which require DGS approval before transferring equipment (and the related records) between State agencies.

### **Recommendation 2**

**We recommend that DHCD**

- a. in conjunction with MDP, investigate the equipment items that could not be located, and request write-off approval from DGS, as warranted;**

- b. refer the matter to the Office of the Attorney General – Criminal Division, if it concludes that any missing equipment items may have been misappropriated; and
- c. after obtaining any necessary approval from DGS, transfer the aforementioned property and equipment records to MDP.

**Finding 3**

**DHCD had not established adequate accountability and control over its equipment.**

**Analysis**

Adequate control and accountability was not established over equipment. According to DHCD's records, as of June 30, 2008, equipment totaled approximately \$6.2 million. We noted the following conditions:

- A physical inventory of both sensitive and non-sensitive equipment conducted in April 2008 had not been reconciled to the detail records as of October 2008. Furthermore, according to DHCD's records, prior to conducting this inventory, the last physical inventories of sensitive and non-sensitive equipment items were completed in August 2004 and April 2002, respectively.
- As of June 30, 2008, DHCD's equipment balance recorded in the State's accounting records (\$7.7 million) exceeded DHCD's equipment control records (\$6.2 million) by approximately \$1.5 million. DHCD has determined that this difference is mainly due to duplicate entries in FMIS. We were advised by DHCD management that it is in the process of correcting this difference.

The DGS *Inventory Control Manual* requires that the results of physical inventories be reconciled with the related detail records. The *Manual* also requires that inventories of sensitive items be taken at least once each year and of non-sensitive items be taken at least once every three years. Furthermore, the Comptroller of the Treasury's General Accounting Division *Accounting Procedural Manual* states that State agencies must enter data accurately and timely into the State's records and make necessary adjustments to eliminate unnecessary transactions.

### **Recommendation 3**

**We recommend that DHCD**

- a. comply with the aforementioned requirements of the *DGS Inventory Control Manual* by conducting physical inventories at required time intervals,**
- b. reconcile the results of the physical inventories to the related detail records, and**
- c. process the necessary adjustments to the State's records to accurately reflect the value of its equipment.**

### **Year-End Closing Transactions**

#### **Finding 4**

**DHCD recorded accrued federal fund revenues totaling approximately \$663,000 for which funding may not be available.**

#### **Analysis**

For the fiscal year ending June 30, 2008, and also for the fiscal year ending June 30, 2007, DHCD recorded accrued federal fund revenues totaling approximately \$663,000 for which funding from the related federal grant is no longer available. DHCD advised us that these accruals were the result of accounting errors, such as allocation of expenditures, dating back several years, and it believes that sufficient funds will be available to fund these expenditures through other federal grants. Since these accrued revenues were recorded to offset existing expenditures previously charged to federal funds, if additional federal authorization is not attained, State general funds may be needed to eliminate the resulting deficits.

The closing instructions issued by the Comptroller of the Treasury's General Accounting Division require that revenue should be accrued only when revenues are measurable and available (collectible within 60 days of the end of the fiscal year).

#### **Recommendation 4**

**We recommend that, in the future, DHCD refrain from recording accrued revenues for which funding may not be available.**

## **Audit Scope, Objectives, and Methodology**

We have audited the following units of the Department of Housing and Community Development (DHCD) for the period beginning July 1, 2005 and ending June 30, 2008:

Office of the Secretary  
Division of Finance and Administration  
Division of Information Technology

The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine DHCD's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations. We also determined the status of the findings contained in our preceding audit report.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of materiality and risk. Our audit procedures included inquiries of appropriate personnel, inspections of documents and records, and observations of DHCD's operations. We also tested transactions and performed other auditing procedures that we considered necessary to achieve our objectives. Data provided in this report for background or informational purposes were deemed reasonable, but were not independently verified.

Our audit included certain support services (such as payroll, maintenance of accounting records, and related fiscal functions) provided by DHCD's Division of Finance and Administration to other units of DHCD.

Our audit did not include an evaluation of internal controls or an assessment of DHCD's compliance with federal laws and regulations pertaining to federal financial assistance programs because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including DHCD.

DHCD's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes a finding relating to a condition that we consider to be a significant deficiency in the design or operation of internal control that could adversely affect DHCD's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to DHCD that did not warrant inclusion in this report.

DHCD's response to our findings and recommendations is included as an appendix to this report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DHCD regarding the results of our review of its response.

## APPENDIX



MARTIN O'MALLEY  
*Governor*  
ANTHONY G. BROWN  
*Lt. Governor*  
RAYMOND A. SKINNER  
*Secretary*  
CLARENCE J. SNUGGS  
*Deputy Secretary*

February 17, 2009

Mr. Bruce A. Myers, CPA  
Legislative Auditor  
Department of Legislative Services  
Office of Legislative Audits  
301 West Preston Street, Room 1202  
Baltimore, MD 21201

Dear Mr. Myers:

Enclosed please find our response to the legislative audit report of the Office of the Secretary, Division of Finance and Administration and Division of Information Technology within of the Department of Housing and Community Development (DHCD) for the period beginning July 1, 2005 and ending June 30, 2008.

I have reviewed the findings and recommendations contained in the report and have committed the DHCD to a plan of corrective action, which is summarized in the attachment. Additionally, our plan of action documents the approximate time frame for compliance with the audit report's recommendations.

The DHCD views the correction of legislative audit findings with the utmost seriousness. You can be assured that every action will be taken to ensure compliance with the audit's recommendations. If you have any questions regarding our response, please do not hesitate to contact me or Mr. Leroy Rose, Internal Audit Manager, at 410 514-7032 or at [rose@mdhousing.org](mailto:rose@mdhousing.org).

Sincerely,

Raymond A. Skinner  
Secretary

Attachment(s)

cc: Mr. Leroy Rose, Internal Audit Manager, DHCD



## **DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT (DHCD)**

### **Responses to Findings and Recommendations Contained in the Legislative Audit Report of the Department**

**For the Period Beginning July 1, 2005 and Ending June 30, 2008**

**Finding 1** – **The Department of Housing and Community Development (DHCD) did not ensure that all funds due to the Maryland Affordable Housing Trust (MAHT) were received and that all grantee reports were obtained.**

**Response** - DHCD concurs with the finding and recommendations. It should be noted that DHCD established procedures in 2006 to ensure annual reports were submitted, which included coordination with the Enforcement Unit of the Maryland Insurance Administration (MIA), in response to a previous audit finding. Recognizing the need to further improve these procedures, DHCD began the process of implementing a database in spring 2008, prior to the start of the latest legislative audit. To make the process more efficient, DHCD created a database to capture both the information received from the banks throughout the year, and the information contained in the annual reports received from the title companies. This database is now fully implemented and has significantly improved the efficiency and effectiveness of the reconciliation process, as well as the identification of non-reporting title companies.

However, the implementation of the database caused a delay in the input of the 2007 annual reports submitted by the title companies and therefore the reconciliation to the remittances received throughout the year from the banks was also delayed. The initial input of annual reports and reconciliation for calendar year 2007 was completed in November 2008. As of February 13, 2009, 77 letters have been sent to title companies with identified reconciling differences in excess of the established threshold. DHCD has been steadily receiving responses to those letters and the identified differences have been resolved. DHCD established controls to track responses and attempts to contact unresponsive title companies at least twice, after which unresponsive title companies will be referred to MIA for further compliance follow-up. DHCD is anticipating a timely reconciliation of the 2008 annual reports, which are due from the title companies on March 31, 2009.

In order to address the significant backlog of non-reporting title companies from prior years, DHCD consolidated the 2005 through 2007 data for all non-reporting title companies and submitted it to MIA on December 10, 2008. DHCD had previously submitted smaller batches of non-reporting title companies at MIA's request. MIA continues to investigate the complaints from MAHT on non-reporting title companies and has initiated consent orders with some of those companies for failing to follow Insurance regulations. To title companies, a consent order is preferable to revocation of their license; most consent orders include instructions to repay amounts due to MAHT. To date, DHCD has received approximately \$27,000 from title companies that have signed consent orders with MIA. DHCD will continue to work with MIA on an ongoing basis to follow up on all non-reporting title companies. DHCD is also in discussion with MIA regarding certain changes to the regulations that DHCD believes will provide better compliance by title companies.

DHCD believes the most efficient and effective way to address the service charge compliance issue is for MAHT to request that the financial institutions provide an itemized statement of each service charge

assessed as permitted under MIA Regulation 31.16.03.04A(2)(b) and is revising its reporting procedures to require this information.

DHCD has implemented a process to follow up on required grantee reports that are not submitted in a timely manner, and will not disburse funds to any grantee having outstanding reports. A timely submission of required reports for prior funding is now an important factor in future funding decisions.

**Finding 2 – Records for property and equipment totaling approximately \$25.7 million had not been transferred to the Maryland Department of Planning (MDP).**

**Response** - DHCD concurs with the finding and recommendation. DHCD has already begun the implementation of a corrective action plan that was reviewed by the Office of Legislative Audits in September, 2008. The \$25.7 million of property and equipment related to the transfer of the Division of Historical and Cultural Programs (DHCP) from DHCD to MDP. As indicated during the audit, DHCD did not transfer these fixed assets previously, since MDP was unable to transfer the fixed assets into their records. DHCD retained the fixed assets on their records in order to ensure that these substantial fixed asset records continued to be maintained and reported in the State's Comprehensive Annual Financial Report.

DHCD and MDP have met and agreed on an action plan for the transfer of the property and the equipment. Since all property is in the name of the Maryland Historical Trust, no title work needs to be completed prior to the completion of the transfer. MDP has contacted the Department of Information Technology to arrange for training on the R\*STARS Fixed Asset Subsystem (FASS) that will enable MDP to transfer the assets into their agency. Upon completion of the training, the land, buildings and construction in progress will be transferred.

As discussed during the audit, in anticipation of the October 1, 2005 transfer of DHCP to MDP, DHCD performed a complete physical audit of DHCP's equipment in conjunction with DHCP staff in April 2005, tagging the DHCP equipment with unique asset tags. Subsequent to the transfer, MDP performed its own physical inventory and retagged the equipment with MDP asset tags. DHCD and MDP are in the process of conducting a joint physical inventory of equipment that will compare the property tags of both agencies, identify any differences, and proceed with any actions needed, including obtaining required approvals from the DGS.

**Finding 3 – DHCD had not established adequate accountability and control over its equipment.**

**Response** - DHCD concurs with the finding and recommendations. DHCD has already begun the implementation of a corrective action plan that was reviewed by the Office of Legislative Audits in September, 2008.

DHCD worked with the Department of General Services Inventory Standards and Support Services Division (ISSSD) to review all surplus furniture and equipment. All appropriate excess property declaration forms have been completed. Some of the surplus was deemed to be unserviceable by ISSSD and disposition has been completed in accordance with regulations. All serviceable surplus is now in the process of being posted to GovDeals.com. All surplus assets will be removed from the R\*STARS

FASS after final approval is received from ISSSD, once the property has either been sold as a result of the postings or the posting period on GovDeals.com has expired. DHCD will correct the duplicate entries in FMIS by the end of fiscal year 2009.

Once the MDP physical inventory and reconciliations are completed, DHCD will conduct a complete physical inventory of furniture and equipment; reconcile with the inventory records; identify any differences; and process any necessary transactions to accurately reflect the value of its equipment. Future physical inventories will be completed in accordance with the DGS *Inventory Control Manual*.

**Finding 4** – DHCD recorded accrued federal fund revenues totaling approximately \$663,000 for which funding may not be available.

**Response** - DHCD concurs with the finding and recommendation. This accrual represented an accounting error; DHCD should have recorded a transfer between three Section 8 Programs instead of accrued revenue, as this balance was the result of inappropriately allocated expenses. DHCD completed a correcting transaction on December 22, 2008 that eliminated the incorrectly recorded accrued revenue. No general funds or special funds were used in the transaction.

AUDIT TEAM

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