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To C.J. Niles, Director of the
Department of Economic Development:

As a result of alleged irregularities at Neighborhood Housing Services of Des Moines, Inc. (NHSDM) and at your request, we conducted a special review of records related to Local Housing Assistance Program (LHAP) funds granted to NHSDM by the Department of Economic Development. We have applied certain tests and procedures to selected financial transactions of NHSDM for the grant period of January 19, 2000 through January 31, 2002. Based on discussion with NHSDM personnel and review of relevant information, we determined the following information.

NHSDM applied for a LHAP grant in July, 1999 and was subsequently awarded \$333,825 to provide assistance to low-moderate home buyers and existing homeowners with home improvements and repairs by offering low-interest mortgages. NHSDM submitted an administrative plan to the Department for the "Homeownership and Home Improvement Loan Program" to be funded with the LHAP funds. The administrative plan was received by the Department in November, 2000, and it outlines the eligibility requirements of the program. Those eligibility requirements include:

- (a) The applicant's/borrower's gross annual income shall not exceed, at initial application, 80% of the City of Des Moines and/or Polk County median family income limits.
- (b) The applicant/borrower must have the ability to meet the underwriting guidelines of the program.
- (c) The applicant/borrower must presently reside in and/or presently work in Polk County.
- (d) The applicant/borrower must not have more than \$25,000 total liquid assets.
- (e) The applicant/borrower must be a United States citizen or a non-citizen that has eligible immigration status.
- (f) The program area will include all residential land use areas of Polk County.
- (g) The property must be either a "for sale" owner-occupied single-family dwelling, as defined by local zoning ordinance, or a rental property "for sale" and vacant.
- (h) The property structure must be a single-family dwelling unit, townhouse, or modular home. Condominium units must be Fannie Mae approved to be eligible. Manufactured homes must be placed on a permanent foundation to be eligible.
- (i) The purchase price limit of a home under the program cannot exceed the LHAP limits of \$120,000.

- (j) The property must meet the Housing Quality Standards established by the Department of Housing and Urban Development (HUD) prior to purchase and/or after home improvement.
- (k) The property purchased must meet all local city and/or county residential codes.
- (l) The applicant/borrower must live in the unit as an owner-occupant.
- (m) The applicant/borrower shall not own or have any interest in any residential property other than that for which an application is being submitted.

In addition, NHSDM requested in the administrative plan that funds re-paid to the program be used for continued (revolving) lending activities throughout the county for persons who do not exceed the 80% of median family income requirement. According to the plan, NHSDM intended to sell the loans to the secondary market through Neighborhood Housing Services of America (NHSA) and continue to revolve the funds to assist other applicants/borrowers.

Based on discussions with Department and NHSDM personnel, and a review of relevant information, we performed the procedures listed below and drew the following conclusions.

- (1) We attempted to review NHSDM's policies and procedures to determine whether adequate policies and procedures were in place and operating effectively to administer the Homeownership and Home Improvement Loan Program.

We were unable to review the policies and procedures due to change in staff and lack of documentation of the policies and procedures in place at the time of the issuance of loans under LHAP.

- (2) We obtained a list of loans issued by NHSDM using LHAP funds.

Based on the records we reviewed, NHSDM issued five home loans totaling \$317,090 with the LHAP grant funds. The following table summarizes the five loans.

Loan Number	Borrower(s)	Property Address	Interest Rate	Purchase Price	Amount of Loan
2011*	Eric J. Allen	2222 Swan Dr. Norwalk, IA	6%	\$ 89,000	19,200
13994*	Teresa M. Pearson	601 East DeWitt Pleasantville, IA	6%	89,750	37,100
13292^	David Thornton & Michelle Hopkins	2849 Rutland Des Moines, IA	3%	99,900	102,890
2020^	Michelle Warne	1550 23 rd St. Des Moines, IA	6%	46,000	56,000
-^	Arturo & Sara Zamaro	1140 21 st St. Des Moines, IA	2%	100,000	101,900
Totals				\$ 424,650	317,090

* - A portion of the purchase price was financed by a loan from USDA.

^ - Financing included funds for improvements and repairs to home being purchased.

The audit report for the year ended December 31, 2000 shows that \$16,691 of the LHAP funds were received for administrative expenses. This is in compliance with IAC 261-28.8(2) which allows recipients to use up to five percent of a total LHAP award for administrative costs. The remaining balance of the grant (\$43.75) was not identified.

- (3) We reviewed the application files for the five loans to determine compliance with the eligibility criteria listed above.

We identified the following non-compliance issues for the five loans.

- Two of the loans were for property located outside of Polk County. One property was located in Warren County and one was located in Marion County.
- The files for the five loans did not contain documentation of an inspection performed to determine that the home met Housing Quality Standards (HQS).
- Formal approval of the five loans was not documented in the application files. According to discussions with NHSDM staff, the Executive Director, Kathleen Moretz, approved all loans issued by NHSDM; however, questionable loans were forwarded to a loan committee for review and approval. Minutes of the loan committee meetings could not be located for the time period in which the loans were issued. We were unable to determine whether the loans were submitted to the committee for review or by whom they were approved.
- Loan number 13292 was processed by a loan officer employed by NHSDM that was the sister of one of the borrowers. Also, the realtor involved in the transaction was a member of NHSDM's Board of Directors. We did not identify any other loans that were issued to family members of NHSDM staff members.
- The administrative plan submitted to the Department of Economic Development stated that loans with interest rates ranging from three to six percent would be offered. As illustrated in the preceding table, loans issued with LHAP funds had interest rates of two to six percent. We were unable to determine the policies and procedures used for setting the interest rate applied to each loan. According to NHSDM staff, interest rates were set by Executive Director Kathleen Moretz.

- (4) We attempted to determine how LHAP funds were used once they were repaid to NHSDM.

Three of the five loans were sold to NHSA. Because NHSDM did not track the proceeds from the sale of the three loans, the funds lost their identify as LHAP grant funds. As a result, we were unable to determine whether the funds were used in accordance with the grant agreement. Loans sold to NHSA were sold at par at the date of sale. As summarized in the following table, the loans were sold for a total of \$194,904.56.

Loan Number	Borrower(s)	Amount of Loan	Proceeds from Sale of Loan
2011	Eric J. Allen	\$ 19,200.00	-
13994	Teresa M. Pearson	37,100.00	36,948.15
13292	David Thornton & Michelle Hopkins	102,890.00	102,181.09
2020	Michelle Warne	56,000.00	55,775.32
-	Arturo & Sara Zamaro	101,900.00	-
Totals		\$ 317,090.00	194,904.56

The Department should attempt to recover the remaining Local Housing Assistance Program funds that are held by Neighborhood Housing Services of Des Moines. Because NHSDM ceased operations at the local office on October 31, 2002, we recommend that you contact Donna Garcia, Program Specialist for Affordable Housing Consultants, to resolve this issue.

According to a minutes of the Board of Directors' meeting held on October 22, 2002, the two remaining loans were to be assigned to the Department of Economic Development. It is our understanding that the Board will ensure arrangements are made to have the loan holders begin submitting loan repayments to the Department.

While most of our fieldwork was completed in July, we remained in contact with NHSDM during August to obtain additional information and resolve pending issues. In early September, we requested a representation letter from NHSDM officials acknowledging that all records and information were provided during our review. However, as of December 2, 2002, a completed representation letter has not been provided to us.

The procedures described above do not constitute an audit of financial statements conducted in accordance with U.S. generally accepted auditing standards. Had we performed additional procedures, or had we performed an audit of the financial statements of Neighborhood Housing Services of Des Moines, Inc., other matters might have come to our attention that would have been reported to you.

We would like to acknowledge the assistance and many courtesies extended to us by the personnel of the Department of Economic Development and Neighborhood Housing Services of Des Moines, Inc. during the course of our review.

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cc: Donna Garcia