



U.S. DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT
OFFICE OF INSPECTOR GENERAL

April 20, 2015

MEMORANDUM NO:
2015-PH-1805

Memorandum

TO: William A. Wilkins
Director, Office of Public Housing, Chicago Field Office, 5APH

//signed//

FROM: David E. Kasperowicz
Regional Inspector General for Audit, Philadelphia Region, 3AGA

SUBJECT: The Chicago Housing Authority, Chicago, IL, Did Not Always Make Payments for Outside Legal Services in Compliance With Requirements

INTRODUCTION

We conducted a review of the Chicago Housing Authority's payments for outside legal services in conjunction with an ongoing internal audit of the U.S. Department of Housing and Urban Development's (HUD) oversight of public housing agencies' expenditures for outside legal services. Our review objective was to determine whether the Authority made payments for outside legal services in compliance with applicable requirements.

METHODOLOGY AND SCOPE

The Authority was one of three Moving to Work housing authorities we selected for review as part of our ongoing internal audit. To accomplish our review objective, we identified payments that the Authority made from October 1, 2007, through September 30, 2012, for outside legal expenses. We determined that the Authority incurred outside legal expenses in two ways. It made payments directly to outside law firms for services rendered, which we classified as direct payments. It also authorized private property management firms to make payments on its behalf for outside legal services. We classified those payments as indirect payments.

We determined that the Authority made \$2.1 million in direct payments related to 503 invoices and \$5.4 million in indirect payments related to 10,038 invoices for outside legal services during the review period. We statistically selected 81 sample invoices totaling \$774,601 for the direct payments and 110 sample invoices totaling \$141,475 for the indirect payments. We requested

the Authority provide the documentation supporting its payment of the sample invoices. In addition, we obtained and reviewed the following:

- Relevant HUD regulations and requirements.
- Invoices, canceled checks, contracts, and purchase orders related to direct payments that the Authority made to 12 outside law firms.
- Invoices, canceled checks, contracts, purchase orders, general journal entries, and general ledger entries related to indirect payments made on behalf of the Authority by property management firms to 11 outside law firms.
- The Authority's record retention policy, private property management procedural manual, and private property management financial policy manual.
- The Authority's Moving to Work agreement and its administrative plans with Moving to Work certifications.

We also held discussions with HUD program officials and Authority officials.

We used statistical sampling procedures to estimate the potential unsupported payments related to the universes for direct and indirect payments based on issues identified.

Our review covered transactions and events that occurred during the period October 1, 2007, through September 30, 2012. This was a limited scope review. Therefore, it was not performed in accordance with generally accepted government auditing standards.

BACKGROUND

The U.S. Housing Act of 1937, as amended, initiated the Nation's public housing program. That same year, the City of Chicago established the Chicago Housing Authority under Illinois laws to provide decent, safe, and sanitary housing. The Authority's main administrative office is located at 60 East Van Buren Street, Chicago, IL. The Authority is governed by a 10-member board of commissioners. The board is responsible for overseeing the Authority's operations as well as the review and approval of its policies. The Authority is the Nation's third largest public housing authority and owns and operates approximately 21,200 public housing units. The Authority's chief executive officer is appointed by the mayor and is responsible for supervising and managing all of the Authority's operations, programs and activities.

The Authority is a participant in HUD's Moving to Work Demonstration program. In 1996, Congress authorized the Moving to Work Demonstration program as a HUD demonstration program. This program allowed certain housing authorities to design and test ways to promote self-sufficiency among assisted families, achieve programmatic efficiency, reduce costs, and increase housing choices for low-income households. Congress exempted participating housing authorities from much of the United States Housing Act of 1937 and associated regulations as outlined in the Moving to Work agreements. Participating housing authorities have considerable

flexibility in determining how to use Federal funds. In February 2000, the Authority signed its Moving to Work agreement with HUD and was accepted into the program. In June 2008, HUD entered into a new 10-year Moving to Work agreement with the Authority. The new agreement expires in December 2018. The Authority's fiscal year begins on January 1.

RESULTS OF REVIEW

The Authority did not always make payments for outside legal services in compliance with applicable requirements. It paid for legal services that were not within contract terms and did not always maintain adequate documentation to support payments for legal services. These problems occurred because the Authority lacked controls to ensure that it adequately verified invoices before payment and followed Federal requirements, contract terms, and its own internal record retention policies. As a result, it made \$503,744 in unsupported payments for outside legal services. The unsupported payments included \$362,549 in direct payments (see appendix C for details) and \$141,195 in indirect payments.

The Authority Paid for Legal Services That Were Not Billed in Accordance With Contract Terms

The Authority made \$259,596 in direct payments for legal services that were not billed in accordance with contract terms. It paid for services rendered by unapproved personnel and services based on block billing, general billing descriptions, and unbillable charges that were explicitly prohibited. Regulations at Office of Management and Budget Circular A-133, subpart C.300(c), required the Authority to comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs. Regulations at 24 CFR (Code of Federal Regulations) 85.36 required the Authority to ensure that contractors performed in accordance with the terms, conditions and specifications of their contracts. Also, the Authority's outside billing guidelines, which were part of each individual contract, indicated that law firms would be paid only for allowable and reasonable expenses and that the Authority would not pay for certain expenses, such as, intraoffice conferences, duplication of legal services by multiple staff, and improper billing of professionals' time. The Authority lacked controls to ensure that it adequately verified invoices before payment and followed Federal requirements and contract terms and as a result, made \$259,596 in direct payments for legal services that were not billed in accordance with the contract. The following paragraphs provide details.

The Authority Paid for Legal Services That Were Performed by Unapproved Personnel

According to article 2, section 2.03, of the contractual agreement between the Authority and outside law firms, key personnel needed to be approved by the Authority's Office of General Counsel before performing legal services, and the Authority would not pay for legal services performed by personnel who were neither listed in the contract nor approved by its Office of General Counsel. However, of the 81 invoices associated with direct payments reviewed, 37 totaling \$159,985 reflected legal services performed by unapproved personnel. The Authority stated that it could not always comply with the contracts because it did not always know what personnel would be available to perform legal services. However, as a result of our review, the Authority stated that it would include a provision in future contracts to require any personnel not

listed in the contract to be added to a task order before performing legal work. To resolve this issue, the Authority needs to provide additional documentation to HUD to support the payments totaling \$159,985 or repay applicable programs for any costs that it cannot support.

The Authority Paid for Legal Services Based on General Descriptions of Services

The Authority's outside billing guidelines stated that the use of vague or generally described activities on an invoice was unacceptable and would not be compensated. However, we identified 24 invoices totaling \$55,669 that reflected general descriptions of services. The general descriptions included line items such as "setting up meeting" or general discussions that lacked detail. A sample excerpt from an invoice reflecting general descriptions of services performed is shown in appendix F. To resolve this issue, the Authority needs to provide additional information and documentation to HUD to support the payments totaling \$55,669 or repay applicable programs for any costs that it cannot support.

The Authority Paid for Unbillable Charges

The Authority's outside billing guidelines stated that it would not pay for certain expenses, such as intraoffice conferences, duplication of legal services by multiple staff, and improper billing for professionals' time. However, we identified eight invoices totaling \$32,429 that reflected charges for intraoffice conferences, duplication of services by multiple staff, legal services without required advance approval, and improperly billed legal services due to incorrect billing rates. A sample excerpt from an invoice reflecting an unbillable charge for intraoffice conferences is shown in appendix D. To resolve this issue, the Authority needs to provide additional documentation to HUD to support the payments totaling \$32,429 or repay applicable programs for any costs that it cannot support.

The Authority Paid for Legal Services Based on Prohibited Block Billing

Contrary to its contract terms, the Authority made payments for invoices that reflected block-billed entries. The Authority's outside billing guidelines stated that it would not pay for "blocked time entries," which include a single time charge for multiple activities. However, we identified 15 invoices totaling \$11,513 that reflected block-billed time entries. This type of billing does not identify the nature of the work performed; therefore, it was impossible to identify how much time was spent on an activity to determine the reasonableness, necessity, and accuracy of the work performed. A sample excerpt from an invoice reflecting block billing is shown in appendix E. To resolve this issue, the Authority needs to provide additional information and documentation to HUD to support the payments totaling \$11,513 or repay applicable programs for any costs that it cannot support.

The Authority Did Not Provide Adequate Support for Payments for Outside Legal Services

The Authority failed to provide adequate documentation to support about \$102,953 in direct payments it made for outside legal services. It could not demonstrate that the legal services invoiced and related payments it made were in accordance with contract terms and HUD requirements. Regulations at 2 CFR Part 225, appendix (C)(1)(j), state that to be allowable

under Federal awards, costs must be adequately documented. However, the Authority failed to adequately support its expenditures for outside legal services with the appropriate documentation. The Authority provided some supporting documents for its expenditures; however, the documentation lacked one or more of the following elements required by the respective contracts:

- Prior approval of the use of consultants,
- Prior approval for legal research hours and cost,
- Prior approval from HUD for service extension,
- Prior approval for deposition costs and supporting documentation for costs,
- Charges for time spent making telephone calls and on correspondence to copy services providers,
- Support for copy expenses, and
- Support for payment approvals.

To resolve these issues, the Authority needs to provide additional documentation to HUD to support the payments totaling \$102,953 or repay applicable programs for any costs that it cannot support.

The Authority Failed To Maintain Source Documentation for Its Indirect Payments for Outside Legal Services

The Authority could not provide source documentation for \$141,195 in indirect payments it made for outside legal services. Under its Moving to Work certifications, the Authority certified that it would comply with regulations at 24 CFR 85.20(b), which state that accounting records must be adequately supported by source documentation, such as canceled checks, paid bills, contracts, and subgrant award documents. However, the Authority generally could not provide complete documentation, including contracts, purchase orders, checks, and other financial records, for the indirect payments sample, consisting of 110 payments totaling \$141,475. It provided only 80 invoices, 1 contract related to 7 invoices, and 41 purchase orders. Only two sample payments totaling \$280 were completely supported. Because it failed to provide complete documentation for almost all the sample items, we could not determine whether the \$141,195 that the Authority spent was for allowable and reasonable expenses.

The Authority's record retention policy required that contracts and agreements be maintained for 12 years and paid bills, invoices, canceled checks, and check registers be maintained for 9 years. However, the Authority stated that it did not have the documentation we requested because it had stopped doing business with most of the property management firms that made the payments for legal services on its behalf. The Authority lacked controls to ensure that it complied with its record retention policy when it stopped doing business with property management firms. As a result of our review, the Authority planned to begin monitoring litigation performed on its behalf by property management firms. The Authority also planned to switch from outside to in-house counsel for litigation related to evictions.

To resolve this issue, the Authority needs to provide additional documentation to HUD to support the payments totaling \$141,195 or repay applicable programs for any costs that it cannot support.

Conclusion

The Authority did not always make payments for outside legal services in compliance with applicable requirements. It lacked controls to ensure that it adequately verified invoices before payment and followed Federal requirements, contract terms, and its own record retention policies. As a result, it made unsupported payments totaling \$503,744 for outside legal services.

Based on our results, we estimated that at least \$924,085 of the \$2.1 million of the Authority's direct payments for outside legal services could be unsupported. Also, we estimated that at least \$4.9 million of the \$5.4 million of the Authority's indirect payments for outside legal services could be unsupported.

RECOMMENDATIONS

We recommend that the Director of HUD's Chicago Office of Public Housing require the Authority to

- 1A. Provide documentation to support the \$503,744 in unsupported payments identified by the review or reimburse the applicable programs from non-Federal funds for any costs that it cannot support.
- 1B. Develop and implement controls to ensure that invoices for legal services are adequately verified and ensure that its payments for outside legal services are made in accordance with the terms of the related contracts and other applicable requirements.

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS

Recommendation number	Unsupported 1/
1A	\$503,744

- 1/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation


Auditee Comments

Comment 1

Comment 1

Comment 2

Comment 3



CHA
CHICAGO HOUSING
AUTHORITY

Z. Scott
Chairperson

Matthew Brewer
Mark Cozzi
Dr. Mildred Harris
Harriet Johnson
John G. Markowski
M. Bridget Reilly
Rodrigo A. Sierra
Francine Washington
Board of Commissioners

Michael R. Morshant
Chief Executive Officer

Chicago Housing Authority
60 E. Van Buren
12th Floor
Chicago, IL 60605
312-742-7500
www.thecha.org

March, 27, 2015

Mr. David E. Kasperowicz
Regional Inspector General for Audit
HUD Office of the Inspector General
Philadelphia Regional Office
U.S. Department of Housing and Urban Development
Office of the Inspector General

Re: Draft Audit Memorandum No. 2015-PH-180X ("Draft Memorandum")

Dear Mr. Kasperowicz:

This correspondence is the follow-up to our March 19, 2015 exit conference call discussion of the above referenced Draft Memorandum with respect to recommendations and findings of the U.S. Department of Housing and Urban Development ("HUD") Office of the Inspector General ("OIG") in its audit of payments by the Chicago Housing Authority's ("CHA") for outside counsel legal services during the period of October 1, 2007 through September 30, 2012 ("Audit Period"). As indicated in the call, this letter contains our written comments to the Draft Memorandum, including elaboration of comments made during the call.

As partially done in your Draft Memorandum, we would clearly distinguish those payments made directly by the CHA Office of the General Counsel ("OGC") to law firms procured by, contracted with and managed by the CHA OGC; and those identified as "indirect payments" which were made by the CHA's Private Property Managers ("PPMs") to law firms retained by the PPMs, as independent contractors under their property management contracts with the CHA. The OGC's and PPM's clearly procure and manage outside counsel legal services separately and the audit request responses were quite different. Therefore, the analysis of these functions should be separate and distinct and the recommendations should follow suit and clearly delineate between direct and indirect payments.

However, in some statements in the Draft Memorandum, the OIG lumps the direct and indirect payment transactions together, despite the fact that there are clear differences in the audit results of the documentation supplied, and management and controls in place for the two functions. Substantially all of the requested documentation for the invoices, contracts, purchase orders, task orders, payments and supporting documentation for payments made directly by the OGC was supplied. While we acknowledge that there were a few missing or unexecuted documents with respect to direct payments, we dispute with HUD OIG the need for certain additional supporting documentation.

Comment 4

The issue for missing invoices, purchase orders, contracts and supporting documents was mainly with the indirect payments. Some of these issues had been identified by the CHA prior to this audit. The PPMs at a point subsequent to the Audit Period have been required to enter order, invoice and payment documents in the CHA electronic property management system. Moreover, legal services for evictions which comprised a substantial portion of the PPM's requested legal services have been in the process of being transferred to the OGC since 2013. The CHA's Office of the General Counsel is now handling most evictions and has increase its staff from a two person staff of an attorney and paralegal to a three attorneys and a paralegal.

Comment 5

We will first address the comments and recommendations for the direct payment function, which is under OGC management. Most of the findings with respect to direct payments related to the auditor's interpretation of the CHA contracts for outside counsel legal service, the Legal Services Agreements ("LSA"), including the billing guidelines. Findings involve approval of law firm personnel, consultants, research, and depositions, intra-office conferences, general, vague description of services, block billing and unbillable items (eg. Intra office conferences, incorrect billing rates). These will be generally addressed herein with some specific examples.

Comments 4 and 6

The OGC does not lack control but has controls in place for to the payment of legal services. A CHA in house attorney ("Designated Contact") acts as the point of contact for each matter and reviews each invoice from a law firm for the matter and approves the amount to be paid. The invoice payment also requires the approval of the CHA General Counsel. Prior to the Designated Contact review, an invoice may be returned to a law firm by OGC's Management Analyst, if the proper format or general billing guidelines obviously had not been followed.

Authority Paid for Legal Services That Were Performed by Unapproved Personnel

We do not believe there is an applicable regulatory requirement or cost principles that require that individual personnel used by a law firm to perform services under a contract must be pre-approved by the CHA.

Accordingly, CHA disputes the proposed finding that \$159,985 was inappropriately spent on services performed by unapproved personnel. Contracts vary to the extent, if any, that any approval of vendor personnel is required. In fact, the inclusion of such controls is very carefully considered to avoid undermining the vendor's independent contractor status and, in the case of for professional services such as legal services, professional liability.

First, all personnel at a law firm working on a particular matter are, in fact, approved by CHA through the review and approval of invoices. With respect to the approval of personnel handling matters, the LSA lists attorneys and, sometimes, paralegals and provides that "No additional key personnel or authorized personnel shall be added to provide legal services under this Agreement without the express consent of the Office of the General Counsel. The CHA will not pay for any legal services performed by Legal Counsel's personnel who are neither listed herein nor subsequently approved by the Office of the General Counsel."

The listing of the personnel in the originally executed LSA has limitations, for at the time of the contracting, the specific matters are not known and may require additional manpower or particular expertise or experience. Further, over the term of the LSA, generally at least three years and until legal matter assigned during that period are completed, the law firms organizational staffing will probably change. Given the potential dynamics of a matter, staffing

and changes, are discussed with the Designated Contact, who in practice checks personnel billed when reviewing the invoices, avoiding the administrative burdens of additional steps to monitor staffing.

Prior to this audit, the OGC sought to improve monitoring staffing by requiring the law firms to list attorneys to be assigned to that matter in the task order for the matter. However, CHA does not believe that this requirement mandated pre-approval for any changes to that list or render inappropriate work performed by personnel added later. However, in any event, there will still be instances where additional staff may be needed for capacity or for specific expertise or experience in the immediacy of handling a matter including coverage of legal proceedings, when conflicting schedule arise.

Moreover, given the desire to rely upon law firms' professional responsibility for a matter, the law firm's ultimate control over staffing matters must be respected to avoid risk of limiting their liability for any problems with the service provided. It is the law firm itself, not individual attorneys, which are procured, contracted, and which provide professional liability insurance.

The requirement to list participating personnel on the task order was not intended to be a strict liability provision, but a basis to monitor the law firms and determine if the OGC deems it in the best interest of the CHA to continue to assign work to the law firm. The intent is also to incent the firm to proactively manage staffing with the Designated Contact or risk not being paid. Again, nothing in the task order, the contract, or the regulatory scheme requires advance approval of such personnel at the risk of their work being deemed unauthorized.

To hold otherwise places an undue burden on both the CHA and the law firms ability to adequately represent the CHA's interests in critical legal matters.

Last, all of the work specifically identified by the auditors in the category was work that ultimately was approved by CHA and was critical to the defense of its interests.

The Authority Paid for Legal Services Based on General Description of Services

Vague, general descriptions generally have to be considered in the context of the transaction, and other entries in the invoice. We continue to disagree with the auditors on their determination as to what is acceptable description for particular matters.

You have listed five invoices for a firm in the amount of \$38,280 as an unacceptably vague description. As we have indicated, we do not believe these descriptions to be vague and have explained, "These are for a major mixed finance transaction involving multiple parties and many documents. Entries for the most part relate to dealing with specifically identified documents for review, drafting, or negotiation. The "working group calls" are the periodic scheduled calls for the parties and their attorneys to work on comments and issues with the transaction and documents. You must consider billing in the context of the transaction.

Comment 7

Comment 8

Comments 4
and 9

Authority Paid for Unbillable Charges

Charges for intra-office conferences are not prohibited. The guidelines provide "CHA strongly discourages non-essential intra-office conferences, and it will pay for only reasonable amounts of time expended on such conferences on substantive matters. The CHA will not pay for inter-office conferences that are either administrative or educational in nature".

The ability to have intra-office conferences is required to delegate for efficiencies, to effectively utilize firm expertise and to manage team manpower, when necessary.

The example given in appendix D for "CHA-Not-For-Profit formation meeting with J. Cannon, D. Lopez and T. Woods" is a meeting by the partner in charge of this very significant initiative with team associate members, who are working on various tax exempt and legal entity consideration. This is a proper intra-office meeting. It reflects the desired use of less costly associates for cost efficiencies, timely effectiveness. A Designated Contact would analyze the invoice by considering all entries for the meeting and the purposes of the participants by checking their other time entries for the matter. Thus, the charge was reviewed against the standard and deemed to be appropriate.

Disallowance of payments for legal research, merely due to lack of prior approval is not supported by the LSA, nor otherwise required under any regulatory scheme.

Prior approval of Legal Research in excess of two hours is not mandatory. The guidelines provide prior approval "should be" not "must be" done. This works to minimize disputes as to the necessity for extensive research. This provision is to incent law firms to discuss the need for significant research. It also provides a basis for denying charges for research when considered excessive. Because prior approval is nowhere required, CHA believes this finding is insupportable.

The Authority Paid for Legal Services Based on Prohibited Block Billing

The guideline provides "The CHA will not pay for blocked entries, namely a line item with a single time charge for multiple activities". The key is what is considered multiple activities in the context of the matter and the activities being handled but with consideration of practicality, reasonableness, efficiencies, effectiveness and purpose of the extent that break down of activities for billing purposes is warranted for adequate analysis. The purpose is to allow the reviewer to analyze the appropriate aspects of an invoice for the type of matter. As we have indicated there are many instances that we disagree with block billing characterization.

The highlighted entry on Appendix E for "Not-for-Profit corporation; PBCA Incorporation" is of the partner-in-charge for an important CHA initiative for structuring the formation of affiliate(ies) or instrumentality(ies) for real estate development, consulting and other opportunities where a separate entity would be advisable. Given the goal of the task order, it simply is unnecessary to break down the task into multiple subpart and the charge was appropriately reviewed and approved.

Page 4

Comments 4
and 10

Comments 4
and 11

Comment 6

Comments 4
and 12

Comments 4
and 13

Comments 4
and 14

Comments 6, 12,
13, and 14

Comment 15

Comment 16

The Authority Did Not Provide Adequate Support for Payments for Outside Legal Services

Included in this category were expenditures for consultants, legal research, and depositions lacking prior approval. Mandatory prior approval for legal research is not an absolute prerequisite as already discussed. The performance of research in many cases is either the actual assignment or an inherent purpose of the assigned legal matters. During the course of the performance of legal services, the use of consultants as expert advisors, or witnesses is a requisite for the process. As example of consultant approval; materials have been supplied in this audit where greater than \$50,000 in consultant fees are being challenged, that were submitted to OGC by the Corboy firm for approval of a consultant to review and analyze architectural drawings for a lawsuit against an architect in preparations for a mediation and for other proceeding if mediation unsuccessful. The two Designated Contacts in discussions of these materials with the law firm approved the consultant for performing these necessary preparatory tasks.

Depositions to be taken are established in the litigation process, and include those demanded by the opposing party to the CHA. The deposition is taken pursuant to the litigation process and the costs are incurred. For the questioned Grant firm deposition costs, we have provided the documentation supporting the costs, which were approved in the proper process.

With respect to copying, the costs of copying done by a law firm in house does not require a separate invoice, but does when performed by a third party.

We believe that many challenged costs items in issue in this category have been adequately documented and approved for payment.

The Authority Failed to Monitor Source Documentation for Its Indirect Payments for Outside Legal Services (\$141,195)

As we have indicated, prior to the conduct of this audit, the CHA has undertaken steps to improve the process for record keeping for the indirect payment process. Furthermore, we have also reported that prior to this audit, we had reorganized so that the eviction matters, which comprise a majority of the legal matters which were being handled by outside legal counsel retained by the PPMs, are being handled by OGC staff. This reorganization process began in 2013. Although there are the issues with missing documentation, we recommend that we work with HUD to establish that at least some payments can be explored to determine whether these expenses are allowable and reasonable and adequately supported enough to justify the payments.

Conclusion

We agree that there were issues with the records retention for the Property Managers payments of the indirect payments. Property Management is now required to track their orders, invoices and payment in the CHA electronic management system. We will work with HUD to establish the reasonableness and allowability for the payments made. There is no question that legal services for evictions are a legitimate and necessary expense.

Comment 17

With respect to the indirect payments, we have provided adequate documentation with very few exceptions. There is a satisfactory control process in place and that we have been working to enhance. Our process is with the focus on the provision of quality, effective, costs efficient, timely legal services and that law firms are compensated for their provision of such legal services and not on the basis of the perfection of their invoices.

Comment 18

It is our understanding that this response was not to address each item covered under the audit, but to express our comments with respect to the recommendations and findings. We generally are in compliance with the applicable regulatory requirements, but at issue is the interpretation of our contract and its appropriate application to the performance of required legal services. We believe that the audit has proposed some administrative requirements that are not required by either our contracts nor the principals of applicable regulations. Provisions in the LSA intended to incent vendor's behavior to minimize fee disputes, are being interpreted as a basis to prohibit the performance of our payment obligations under the LSA.

Comment 19

We have worked with the audit team to develop their understanding and have respectfully in several instances agree to disagree. In our last previous response we noted there was some determination that we did not understand. We regret that our request for additional time to respond was not granted, limiting the time we had to revisit the audit materials.

We request that you reconsider parts your analysis, findings and recommendation based upon our comments.

We appreciate the cooperation and consideration we have experienced with your audit team and their efforts.

We look forward to the next steps to resolve this matter.

Sincerely,



Scott W. Ammarell
Chief Legal Officer

OIG Evaluation of Auditee Comments

- Comment 1** The Authority stated that the analysis of the direct and indirect payments should be separate and distinct, and the recommendations should follow suit and clearly delineate between direct and indirect payments. We properly distinguished between the two types of payments in the discussion of the issues identified related to the payments. The report clearly identified the deficiencies noted for both payment types. Based on the recommended actions, we do not believe that separate recommendations are needed for direct and indirect payments. We recommended that the Authority provide documentation to support the unsupported payments identified by the review or repay any costs it cannot support from non-Federal funds; and develop and implement controls to ensure that all invoices are adequately verified and all payments are made in accordance with the terms of the contract and other applicable requirements. The Authority needs to work with HUD to determine and take the specific appropriate action required to resolve the issues related to both payment types.
- Comment 2** The Authority stated that it provided substantially all of the requested documentation for its direct payments. However as explained in the report, the review disclosed that it did not provide adequate documentation to support \$362,549 in direct payments for legal services. The unsupported payments represented about 47 percent of the total direct payments reviewed.
- Comment 3** The Authority stated that while it acknowledged that there were a few missing or unexecuted documents with respect to direct payments, it disputed the need for certain additional supporting documentation. It also indicated that it had made some improvements related to the transactions associated with the indirect payments and the accounting process for those payments after the review period. Nevertheless, as discussed in the report, the Authority could not provide adequate documentation to support all of the direct and indirect payments it made during the review period.
- Comment 4** The Authority stated that most of the findings, with respect to direct payments, related to the auditor's interpretation of its contracts for outside counsel legal services, the Legal Services Agreements, including billing guidelines. We reviewed the Authority's contracts and outside billing guidelines. However, we also reviewed several applicable key Federal requirements. The Authority was required to comply with several Federal regulations either directly or by ensuring compliance with its contract provisions and related guidelines. Regulations at Office of Management and Budget Circular A-133, subpart C.300(c), required the Authority to comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs. The Authority's Moving to Work Certificate of Compliance required it to follow requirements from regulations at 24 CFR 85.20 which required that accounting records be

supported by source documentation and adequately maintained. The Authority was also required to follow regulations at 24 CFR 85.36 which required it to ensure that contractors performed in accordance with the terms, conditions and specifications of their contracts. Further, the Authority was required to comply with 2 CFR Part 225, appendix (C)(1)(j), which stated costs must be adequately documented to be allowable under Federal awards.

Comment 5 The Authority stated that its Office of General Counsel did not lack control and had controls in place for the payment of legal services. However as shown in the report, the review disclosed that the Authority made \$503,744 in unsupported payments because it did not adequately verify invoices before payment and follow Federal requirements, contract terms, and its own record retention policies.

Comment 6 The Authority stated that there were no applicable regulatory requirements or cost principles that required it to pre-approve individual personnel prior to performing legal services under a contract. The Authority is correct that there was no regulatory requirement for personnel to be pre-approved prior to performing legal services. However, there was a regulatory requirement for the Authority to follow the terms of its own contract. Regulations at Office of Management and Budget Circular A-133, subpart C.300(c), required the Authority to comply with laws, regulations, and the provisions of contracts or grant agreements related to each of its Federal programs. The contract between the Authority and outside law firms specifically stated that no additional key personnel or authorized personnel would be added or assigned to provide legal services under the contract without the express consent of the Office of General Counsel. The contract also stated that the Authority would not pay for any legal services performed by personnel who were neither listed on the contract nor subsequently approved by the Office of General Counsel. Therefore, the Authority was required to pre-approve personnel before having them performing legal services. The review identified several instances in which personnel were not pre-approved. During the review, the Authority contended that if an attorney was not listed in the contract and pre-approved, they would have been listed on the task order for a legal matter; however, we found that this was not consistently completed. As a result of the review, the Authority stated that it would include provisions in future contracts to require any personnel not listed in the contract to be added to a task order before performing legal work.

Comment 7 The Authority stated that all of the work specifically identified in the unapproved personnel category, was work that it ultimately approved and was critical to the defense of its interests. We did not perform an assessment of the legal work that was performed. Accordingly, we do not express an opinion on whether or not the work performed was critical to the defense of its interests. The issue is that the Authority failed to follow applicable Federal requirements that required it to comply with the provisions of its contracts.

- Comment 8** The Authority stated that vague, general descriptions had to be considered in the context of the transaction and other entries in the invoice, and that it continued to disagree with the audit team’s determination as to what was an acceptable description for particular matters. However, the Authority’s outside billing guidelines clearly stated that the use of vague or generally described activities was unacceptable and would not be compensated. The guidelines also provided specific examples of unacceptable entries, such as those simply reflecting “discussion with” and “conference with” etc. The costs we classified as unsupported were associated with invoices on which we identified time entries which reflected these general descriptions of services for which we were unable to determine the specific tasks or work completed.
- Comment 9** The Authority stated that charges for intra-office conferences were not prohibited. We understand that the contract did not prohibit intra-office conferences; however, as it acknowledged, its outside billing guidelines stated that it strongly discouraged non-essential intra-office conferences, and would only pay for reasonable amounts of time expended on such conferences and conferences on substantive matters. The guidelines also stated that the Authority would not pay for intra-office conferences that were either administrative or educational in nature. Although we provided the Authority several opportunities to do so during the review, it did not provide sufficient information to demonstrate that the costs related to intra-office conferences that we questioned were for substantive matters and not for administrative or educational conferences. The related time entries we reviewed did not include enough information as to what was discussed among the personnel involved. Because we were unable to determine whether the conferences were on substantive matters, we classified the related amounts unsupported.
- Comment 10** The Authority stated that prior approval of legal research in excess of 2 hours was not mandatory. The Authority stated that its guidelines only provided that prior approval “should be” not “must be” done; but rightly acknowledged that the prior approval would minimize disputes as to the necessity for extensive research. The Authority’s outside billing guidelines stated that law firms should obtain prior approval from the Authority’s designated contact before conducting a legal research project that was expected to exceed 2 hours. We agree with the Authority’s position that prior approval would minimize disputes related to the necessity for extensive research. It is a key control to ensure the efficient use of Federal funds. Therefore, the Authority should have ensured that its outside law firms followed this key requirement. For the costs we classified as unsupported, we were unable to determine whether prior approval was given or if any discussions regarding the legal research took place. Also, we were unable to determine from the invoices whether the legal research was necessary or for routine matters.
- Comment 11** The Authority stated that it disagreed with many instances of time entries classified as block billing. The Authority’s outside billing guidelines specifically

stated that it would not pay for “blocked entries,” which include a single time charge for multiple activities. The outside billing guidelines provided examples of an acceptable time charge and what was not an acceptable time charge. The examples in the guidelines showed that if multiple tasks were included in one time entry, the amount of time spent on each task needed to be identified in parentheses next to each component task. During the review, we identified several instances of block-billed time entries. The entries did not identify the specific nature of the work performed or the amount of time spent on each individual component task so we could not determine the reasonableness, necessity, and accuracy of the work performed. As a result, we classified the related costs as unsupported.

Comment 12 The Authority stated that the use of consultants as expert advisors, or witnesses was requisite for the performance of legal services. It also provided an example of a consultant that it approved to review and analyze architectural drawings for a lawsuit against an architect. The Authority’s outside billing guidelines stated that the selection and retention of appraisers, experts, and consultants must be coordinated with and approved by the Authority’s designated contact. However, the Authority did not maintain adequate documentation to show that any approvals were granted for consultants’ work related to the expenses we questioned.

Comment 13 The Authority stated that it properly approved questioned deposition costs for the Grant firm and that it provided the supporting documentation for the costs. However, the Authority failed to properly maintain documentation and did not provide adequate support for either questioned cost. The Authority’s outside billing guidelines stated that copies of invoices for reimbursable expenses should be submitted with the original invoice for professional services. For the deposition costs we questioned, the Authority could not demonstrate that it approved the costs. It also could not provide a copy of the invoice or receipt for one of the costs.

Comment 14 The Authority stated that in-house copying costs did not require a separate invoice. However, although a separate invoice might not be required, the costs still needed to be supported. The Authority failed to provide supporting documentation for in-house copying costs on one invoice. We noted that for in-house copying costs, law firms generally attached to their invoices a computer system print-out that identified the persons who performed the copying, the number of pages, and the dollar amount. However, in the case of the law firm for which we questioned the copying costs, this information was not provided.

Comment 15 The Authority acknowledged that there were issues with missing documentation related to its indirect payments for legal services. It stated that it had undertaken steps to improve record keeping for its indirect payment process, and expressed its willingness to work with HUD to at least resolve some of the unsupported costs associated with the indirect payments. As stated in the report, to resolve the

issue, the Authority needs to provide additional documentation to HUD to support the unsupported indirect payments or repay applicable programs for any costs that it cannot support.

- Comment 16** The Authority stated that legal services for evictions were a legitimate and necessary expense. While we generally agree, we did not review the legitimacy of the Authority's expenses for legal services related to evictions; therefore, we do not express an opinion on the legitimacy of the expenses.
- Comment 17** The Authority stated that with respect to the indirect payments, it had provided adequate documentation with very few exceptions. We disagree. Regulations at 24 CFR 85.20 required that accounting records be supported by adequate source documentation such as, cancelled checks, paid bills, and contract documents. As discussed in the report, the Authority generally could not provide complete documentation, including contracts, purchase orders, checks, and other financial records, for the indirect payments sample, consisting of 110 payments totaling \$141,475. It provided only 80 invoices, 1 contract related to 7 invoices, and 41 purchase orders. Only two sample payments totaling \$280 were completely supported.
- Comment 18** The Authority stated that it generally complied with the applicable regulatory requirements, but the issue was the interpretation of its contract and the appropriate application to the performance of required legal services. However, as discussed in the report, the Authority did not always comply with or ensure compliance with its contract and related billing guidelines as required by Federal regulations. The Authority paid for legal services that were not within contract terms and did not always maintain adequate documentation to support payments for legal services.
- Comment 19** The Authority stated that it regretted that its request for additional time to respond to the review findings was not granted, limiting the time it had to revisit the audit materials. In accordance with our normal practice, we provided the Authority ample time to respond to the review findings. From the time the audit team provided the preliminary review results to the Authority to the time we requested that it provide a written response to the draft report, the Authority had at least 5 months to respond to the review findings. The audit team maintained open communication with the Authority throughout the review and provided it numerous opportunities to discuss and resolve the review findings.

Appendix C

SUMMARY OF DIRECT PAYMENTS BY DEFICIENCY IDENTIFIED

Law firm (16)	Number of invoices reviewed ¹	Total dollar amount	Unsupported amount	No. of invoices with unapproved personnel (1)	No. of invoices with general description (2)	No. of invoices with Unbillable charges (3)	No. of invoices with block billing (4)	No. of invoices with insufficient documentation (5)
Kutak Rock, LLP	17	\$271,702	\$ 60,700	8	0	0	0	4
Mayer, Brown, Rowe & Maw, LLP	12	117,582	90,523	12	4	1	2	0
Corboy & Demetrio, P.C.	6	83,443	83,180	0	0	0	0	6
Charity & Associates, P.C.	7	56,136	43,168	3	5	0	4	1
Grant Schumann, LLC	6	54,171	7,311	0	3	1	0	1
Seyfarth Shaw, LLP	3	37,831	37,368	1	1	2	2	1
Hoogendoorn & Talbot, LLP	2	37,636	11,299	0	1	2	2	1
Hawkins, Delafield & Wood, P.C.	2	32,097	5,669	0	1	1	1	0
Johnson, Jones, Snelling, Gibert & David, P.C.	4	19,743	2,600	2	3	0	0	2
Pugh, Jones, Johnson & Quant, P.C. (PJJQ).	6	18,414	3,953	0	3	0	1	2
Laner, Muchin, Dombrow, Becker, Levin, and Tominberg, LTD	7	13,566	7,016	6	0	0	1	1
Varga, Berger, Ledsky, Hayes & Casey, P.C.	3	12,583	1,826	3	0	1	0	1
Albert, Whitehead, P.C.	3	11,491	0	0	0	0	0	0
Brothers & Thompson, P.C.	1	4,585	4,315	0	1	0	1	0
Schiff Gorman, LLC	1	3,000	3,000	1	1	0	1	1
Hinshaw & Culbertson, LLP	1	621	621	1	1	0	0	0
Totals	81	\$774,601	\$362,549	37	24	8	15	21

¹ Some invoices had more than one deficiency.

(1) Unapproved Personnel:

Lack of supporting documentation to show that a law firm's staff was authorized (approved) to perform legal services according to the contract.

(2) General Description:

A general or vague description of legal services performed. These descriptions lack specificity. Each invoice should describe the parties, the subject, and the purpose, as applicable, for billed services.

(3) Unbillable Charges:

1. Unallowable charges according to the outside counsel billing guidelines (for example, intraoffice conferences or reviewing files not precipitated by an event such as a telephone call); or
2. Inaccurately billed charges (for example, time charges billed at 0.25 of an hour instead of the required 0.10 of an hour).

(4) Block Billing:

1. Only a summary of time charged for each attorney (for example, only attorney name, rate, and total hours and amount billed); or
2. A single time charge for multiple activities performed.

(5) Insufficient Documentation:

1. An invoice was provided, but there was no documentation to support the amount invoiced or paid for services or costs; or
2. An invoice was provided, but the accompanying documentation did not adequately support the amount invoiced or paid.

Appendix D

EXAMPLE OF UNBILLABLE CHARGES

Mayer Brown LLP			
09047446			Page 2
Chicago Housing Authority			
Corporate Issues Re Formation			
<u>DESCRIPTION OF LEGAL SERVICES</u>			
<u>Date</u>	<u>Timekeeper Name</u>		<u>Hours</u>
08/03/09	[REDACTED]	Research related to definition of primary activity in the context of 501(c)(4) organizations (.50), review proposed structure and issues list (.50).	1.00
08/03/09	[REDACTED]	Energy Board financing transaction.	1.50
08/04/09	[REDACTED]	Reviewing 501(c)(3) PLR and Rev. Ruling regarding conducting business as a tax exempt organization.	1.30
08/04/09	[REDACTED]	Conference with [REDACTED] regarding proposed structure for CHA new project and discussion regarding 501(c)(4) status (.25), review and revise 501(c)(4) internal memo (.75).	1.00
08/04/09	[REDACTED]	Bond discussions.	0.80
08/05/09	[REDACTED]	Reviewing memo regarding organization under Internal Revenue Code section 501(c)(4) and corresponding case law (0.70); conference with [REDACTED] to discuss the same (0.20).	0.90
08/05/09	[REDACTED]	Review memo and open issues list regarding proposed structure for CHA special project.	0.50
08/06/09	[REDACTED]	Energy Finance Bond meeting.	2.80
08/06/09	[REDACTED]	Not for Profit corporation.	0.50
08/10/09	[REDACTED]	Reviewing IRS guidance on 501(c)(3) entities entering for profit activities.	0.80
08/10/09	[REDACTED]	Client meeting regarding various formation issues.	1.30
08/12/09	[REDACTED]	Conference with [REDACTED] to discuss structuring issues for CHA affiliate initiative.	0.60
08/12/09	[REDACTED]	Researching filing of Form 1024.	1.30
08/12/09	[REDACTED]	Conference with [REDACTED]	0.80
08/12/09	[REDACTED]	CHA - Not for Profit formation - meeting with J. Cannon, D. Lopez, T. Woods.	1.00
08/13/09	[REDACTED]	Research related to statutes governing low-profit limited liability companies (.50);	1.00

The highlighted example was related to an intraoffice conference among four lawyers. There was no description or explanation to show whether the conference was necessary. The Authority's outside billing guidelines stated that it would not pay for intraoffice conferences.

Appendix E

EXAMPLE OF BLOCK BILLING

Mayer Brown LLP

09047446 Page 3
 Chicago Housing Authority
 Corporate Issues Re Formation

<u>Date</u>	<u>Timekeeper Name</u>	<u>DESCRIPTION OF LEGAL SERVICES</u>	<u>Hours</u>
08/13/09	[REDACTED]	conference with [REDACTED] regarding CHA status update (.50). Not for Profit/LLC formation discussions with client and related follow-up.	0.50
08/14/09	[REDACTED]	Research legislative history and background of low-profit limited liability companies (.50); correspondence to [REDACTED] regarding preliminary findings on low-profit limited liability companies (.15); correspondence to [REDACTED] providing initial draft documentation for not-for-profit corporations (.15).	0.80
08/17/09	[REDACTED]	Tax comments to LPA. Researching 1023 and 1024 filings.	0.50
08/17/09	[REDACTED]	Research regarding low-profit limited liability companies and alternative structures for Illinois not-for-profit entities (2.00), conference with [REDACTED] (.30).	2.30
08/18/09	[REDACTED]	Revisions to open issues memo (.25), correspondence with [REDACTED] regarding open issues memo (.15), correspondence and conference with [REDACTED] regarding updated open issues memo and structuring options (.10), conference at Chicago Housing Authority with [REDACTED] regarding structuring options for new CHA affiliate (2.00).	2.50
08/18/09	[REDACTED]	Not-for-profit corporation; PBCA Incorporation.	2.50
08/20/09	[REDACTED]	Conference with [REDACTED] (.30), revise draft articles of incorporation (.75), conference with [REDACTED] (.10), correspondence to [REDACTED] regarding revised draft articles and open items for formation (.15).	1.30
08/20/09	[REDACTED]	Not-for-profit formation issues.	1.50
08/21/09	[REDACTED]	Not-for-Profit formation issues.	2.30
08/24/09	[REDACTED]	Review bylaws.	0.50
08/25/09	[REDACTED]	Review HUD and inspector general's guidance received from [REDACTED] (.75), review revised bylaws (.25), conference with [REDACTED] regarding selection of board of directors (.25), correspondence with [REDACTED] regarding status of entity formation (.25).	1.50
08/26/09	[REDACTED]	Review board resolution provided by [REDACTED]	0.30
08/26/09	[REDACTED]	Not-for-profit formation issues.	1.50

The highlighted example represented multiple activities billed as a single time charge. There was no description of the activities performed or indication of the time spent on each activity.

Appendix F

EXAMPLE OF GENERAL DESCRIPTION

Mayer Brown LLP

09047446 Page 2
 Chicago Housing Authority
 Corporate Issues Re Formation

Date	Timekeeper Name	DESCRIPTION OF LEGAL SERVICES	Hours
08/03/09	[REDACTED]	Research related to definition of primary activity in the context of 501(c)(4) organizations (.50), review proposed structure and issues list (.50).	1.00
08/03/09	[REDACTED]	Energy Board financing transaction.	1.50
08/04/09	[REDACTED]	Reviewing 501(c)(3) PLR and Rev. Ruling regarding conducting business as a tax exempt organization.	1.30
08/04/09	[REDACTED]	Conference with [REDACTED] regarding proposed structure for CHA new project and discussion regarding 501(c)(4) status (.25), review and revise 501(c)(4) internal memo (.75).	1.00
08/04/09	[REDACTED]	Bond discussions.	0.80
08/05/09	[REDACTED]	Reviewing memo regarding organization under Internal Revenue Code section 501(c)(4) and corresponding case law (0.70); conference with [REDACTED] to discuss the same (0.20).	0.90
08/05/09	[REDACTED]	Review memo and open issues list regarding proposed structure for CHA special project.	0.50
08/06/09	[REDACTED]	Energy Finance Bond meeting.	2.80
08/06/09	[REDACTED]	Not for Profit corporation.	0.50
08/10/09	[REDACTED]	Reviewing IRS guidance on 501(c)(3) entities entering for profit activities.	0.80
08/10/09	[REDACTED]	Client meeting regarding various formation issues.	1.30
08/12/09	[REDACTED]	Conference with [REDACTED] to discuss structuring issues for CHA affiliate initiative.	0.60
08/12/09	[REDACTED]	Researching filing of Form 1024.	1.30
08/12/09	[REDACTED]	Conference with [REDACTED]	0.80
08/12/09	[REDACTED]	CHA - Not for Profit formation - meeting with [REDACTED].	1.00
08/13/09	[REDACTED]	Research related to statutes governing low-profit limited liability companies (.50);	1.00

The highlighted examples did not include clear descriptions of the services performed.