U.S. Department of Housing and Urban Development

OFFICE OF INSPECTOR GENERAL






Top Management Challenges

Facing the U.S. Department of Housing and Urban Development in 2019 and Beyond

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

Memorandum

Date: October 15, 2018

To: Dr. Benjamin S. Carson, Sr.
Secretary, S

From: Helen M. Albert
Acting Inspector General, G

Subject: Management and Performance Challenges for Fiscal Year 2019 and Beyond

Each year, in compliance with Public law 106-531, the Reports Consolidation Act of 2000, the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), issues a report summarizing what we consider to be the most serious management challenges facing the Department. In turn, HUD is required to include it in its annual agency financial report. This report represents HUD OIG's perspective on the top management challenges facing HUD in fiscal year 2019.

HUD's top management challenges result from critical unaddressed internal or external risks, either longstanding or recently emerged. They represent HUD's greatest vulnerabilities to waste, fraud, abuse, and mismanagement or pose significant risk to HUD's ability to achieve its mission. In developing this report, we considered the issues facing HUD and applied our own judgment. This year, we took a different approach to the design and content of this report. We focused on those risks we believe have the greatest potential impact on HUD's ability to succeed. As a result, some issues facing HUD that appeared in previous years' top management challenges are not included in this report, while others are entirely new.

We have identified six top management challenges, listed in no particular order, that impact HUD's ability to meet the needs of its beneficiaries and protect taxpayer dollars:

1. Ensuring the availability of affordable housing that is decent, safe, sanitary, and in good repair
2. Protecting the Federal Housing Administration's mortgage insurance funds
3. Providing adequate monitoring and oversight of its operations and program participants
4. Administering disaster recovery assistance
5. Modernizing technology and the management and oversight of information technology
6. Instituting sound financial management governance, internal controls, and systems

We believe that our revised approach to the top management challenges will be more useful to HUD officials and external stakeholders. Aligning with our mission of identifying opportunities for HUD programs to progress and succeed, this report will also serve as a guiding document for our OIG-wide oversight activities. We look forward to working with HUD to address these critical areas for improvement.

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Introduction

In a general sense, the U.S. Department of Housing and Urban Development (HUD) is meeting its mission to create strong, sustainable, inclusive communities and quality, affordable homes for all. HUD has awarded grants, issued mortgage insurance, provided housing assistance, and performed basic services. Yet HUD continues to demonstrate longstanding performance and accountability issues.

In 1994, the U.S. Government Accountability Office (GAO) placed HUD on its high-risk list because of four longstanding, departmentwide management deficiencies: 1) weak internal controls, such as a lack of necessary data and management processes; 2) poorly integrated, ineffective, and generally unreliable information and financial management systems; 3) organizational deficiencies, such as overlapping and ill-defined responsibilities and authorities between HUD headquarters and field organizations, and a fundamental lack of management accountability and responsibility; and 4) an insufficient mix of staff with the proper skills.[1] Although GAO noted these problems more than 20 years ago, these challenges remain today and are addressed in this report.

Constant turnover and extended vacancies in many of HUD's most important political and career executive positions have created leadership gaps, which have led to poor management decisions and questionable execution of internal business functions. HUD could not fill essential positions with officials who stayed long enough to implement a vision and effect sustained positive changes.

Many, if not all, of HUD's top management challenges are affected by its staffing levels, which have declined substantially since the time of that GAO report. From its highest staffing levels in 1991, HUD's staffing has fallen more than 49 percent.[2] During the 10-year period from 2008 to 2017, HUD lost 18.5 percent of its full-time permanent staff, while the total had increased 11 percent governmentwide.[3] HUD suffered a staffing loss greater than any other cabinet-level department during this time. Not surprisingly, 4 of HUD's top 10 self-identified enterprise risks in 2018 were related to human capital. Many roles previously performed by Federal employees are now outsourced to contractors, leaving fewer Federal employees to perform the inherently governmental responsibilities of performance management, organizational leadership, policymaking, financial management, and monitoring. We intend to conduct more reviews in this area in the future.

With that backdrop, we discuss below what we see as the top six management challenges facing the Department.

[1] As described by GAO report, entitled High Risk Series: Department of Housing and Urban Development, February 1995: https://www.gao.gov/assets/230/220893.pdf
[2] Data collected from HUD as part of the 2018 financial audit
[3] Office of Personnel Management Report, Sizing Up the Executive Branch, February 2018: https://www.opm.gov/policy-data-oversight/data-analysis-documentation/federal-employment-reports/reports-publications/sizing-up-the-executive-branch-2016.pdf

TOP MANAGEMENT CHALLENGE

1

Ensuring the Availability of Affordable Housing That Is Decent, Safe, Sanitary, and in Good Repair

- Affordable Housing
- Safe Housing
- Housing Inspections

Part of HUD's mission is to create quality, affordable homes for all. The housing HUD insures and funds must be decent, safe, sanitary, and in good repair. Economic and demographic factors, as well aging housing stock, have created an extreme shortage of housing that is affordable and safe. HUD's challenge is to adapt existing programs to address ever-increasing housing pressures on the Nation's lowest income residents. A lack of affordable and safe housing is already negatively affecting the health, safety, and well-being of many people. Robust action is needed by HUD to ensure that the quality and quantity of affordable and safe housing increases.

Affordable Housing

HUD has several programs designed to ensure affordable housing for low-income households. The largest of these are public housing and rental housing assistance programs. Although millions of American households are assisted through these programs every year, HUD's Office of Policy Development and Research has found that the supply of rental units that are affordable to very low-income renters is inadequate, with only 62 affordable units available per 100 very low-income renters and only 38 units available per 100 extremely low-income renters.[4] Further, because of the rapid increase in renter households and greater competition, that scarcity of affordable units is now impacting people higher on the income scale.

[4] Worst Case Housing Needs, 2017 Report to Congress, The Office of Policy Development and Research, August 2017

HUD has stated that a family with one full-time worker earning the minimum wage cannot afford the local fair-market rent for a two-bedroom apartment anywhere in the United States.

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HUD's strategies to address affordable housing include promoting economic self-sufficiency programs that will reduce the need for HUD assistance, encouraging public housing agencies (PHA) to transition public housing units to a private-public partnership model, and modifying the rental calculation system "to encourage work and stable family formation."[6] Earlier this year, HUD launched the EnVision Center demonstration to centralize resources from various public and private entities to empower low-income individuals and families to "lead self-sufficient lives." The vision for each center is to help HUD-assisted families sustain economic success, cultivate nontraditional education options, increase access to health and wellness, and assist individuals in reaching their full potential.[7] In addition, in August 2018, HUD established a task force to encourage more landlords to participate in the Housing Choice Voucher Program. We will continue to monitor HUD's efforts to increase the availability of quality, affordable housing as HUD implements these strategies to address this challenge.

Safe Housing

HUD has a strategic goal to remove lead-based paint and other health and safety hazards in housing for families and children. This goal is commendable. Recent events at the New York City Housing Authority (NYCHA), for example, demonstrate the challenge HUD faces in implementing it. For years, NYCHA violated key HUD and U.S. Environmental Protection Agency (EPA) lead paint safety regulations, including failing to inspect apartments for lead paint hazards and remediate peeling lead paint. Work we completed in 2018 supports the fact that HUD did not ensure that PHAs properly reported and mitigated cases involving children with lead contamination, establish policies and procedures for reporting children with lead contamination, or ensure completion of required lead-based paint inspections.[8]

In 2016 and 2017, we reported that HUD did not provide sufficient guidance and oversight to ensure that properties approved for mortgage insurance had a continuing and sufficient supply of safe and potable water.[9] HUD's loan files for properties in areas serviced by public water systems with publicly reported unacceptable levels of

[5] HUD's program definition of affordable housing, https://www.hud.gov/program_offices/comm_planning/affordablehousing/

[6] HUD's strategic plan includes a strategy to "Develop a legislative proposal that modifies the rental calculation system to encourage work and stable family formation, simplifies administration, improves fiscal sustainability, and increases local control and choice." Page 13, https://www.hud.gov/sites/dfiles/SPM/documents/HUDSTRATEGICPLAN2018-2022.pdf

[7] https://www.hud.gov/envisioncenters

[8] Audit Report 2018-CH-0002, HUD's Oversight of Lead-Based Paint in Public Housing and Housing Choice Voucher Programs, issued June 14, 2018

[9] Audit Report 2016-PH-0003, HUD Did Not Ensure That Lenders Verified That FHA-Insured Properties in Flint, MI, Had Safe Water, issued July 29, 2016, and Audit Report 2017-PH-0003, Oversight of Safe Water Requirements for FHA-Insured Loans Nationwide, issued September 29, 2017

contaminants did not provide evidence that the water was tested to ensure that it was safe before issuing the loan. In some cases, properties were later found to have lead and copper levels above EPA's acceptable levels. As a result, HUD could be endorsing loans for properties with contaminants that affect families' health. This issue represents an ongoing safety concern. HUD has said that it intends to address this issue by July 2019.

In addition to the dangers posed by lead in paint and water, some people living in HUD properties have an increased risk of contamination from hazardous waste sites, commonly called Superfund sites.[10] After elevated levels of lead were found in the blood of 21 children at the West Calumet Housing Complex in East Chicago in 2016, HUD worked with EPA to identify its properties nationwide that were near Superfund sites. EPA found that there were 18,158 HUD-assisted buildings within 1 mile of a Superfund site. EPA also found that approximately 41 percent of the sites had not been cleaned, had ongoing human exposure to toxins, had soil contamination, or had no data to determine the exposure status.[11] HUD received this information from EPA in October of 2016, yet it has not conducted an analysis to determine which sites pose the greatest risk to residents, and it has not tested sites to determine whether contaminants exist, which could endanger nearby residents.

In 2017, we began an initiative to investigate cases of children with elevated blood lead levels living in subsidized housing. In March 2018, due to this initiative, we recommended, among other things, that public housing units be tested using wipe samples or x-ray fluorescence spectrum analyzer tests, which are more reliable tests for lead than is currently used; soil samples be analyzed for lead contamination in pre-1978 units; and drinking water be analyzed for lead contamination regardless of the unit's construction date.[12] We plan to continue to produce work products that we believe will provide HUD assistance in addressing this challenge.

Housing Inspections

HUD has a considerable challenge to provide oversight of its properties to ensure that they are decent, safe, sanitary, and in good repair. HUD's Real Estate Assessment Center (REAC) assesses the physical condition of many of HUD's insured and subsidized properties through inspections. We have found instances in which inspection scores rated the physical condition of a property better than it was and as a result, qualified it for less frequent inspections, decreasing oversight. For example, at the Alexander County Housing Authority in Illinois, an artificially high inspection score in 2013 contributed to reduced oversight by HUD, while the true condition of the buildings continued to deteriorate.[13] Only 5 years later, some of the buildings with these inflated scores are scheduled for demolition, and residents have been displaced. This was also the case with inspection scores for residential care facilities (for example, nursing homes,

[10] The Comprehensive Environmental Response, Compensation, and Liability Act, commonly known as Superfund, was enacted by Congress on December 11, 1980. Superfund sites are contaminated sites that exist due to hazardous waste being dumped, left out in the open, or otherwise improperly managed. These sites include manufacturing facilities, processing plants, landfills, and mining sites.

[11] Report entitled EPA/HUD NPL Proximity Analysis, October 2016

[12] Systemic Implication Report number FY17-002, SIR Pertaining to Lead-Based Paint Hazards in Housing, issued March 15, 2018

[13] Evaluation Report 2017-OE-0014, HUD's Oversight of the Alexander County Housing Authority, issued July 24, 2018

assisted living facilities, and board and care homes, etc.), which did not accurately reflect the overall condition of the facilities.[14] Without sufficient and accurate inspections, the living conditions for residents may degrade, and the value of the collateral HUD insures may decline.

REAC relies on contractors to inspect HUD-assisted properties. In a recent audit, we looked at HUD's processes for and controls over the certification and monitoring of contracted inspectors. HUD is not ensuring that the people inspecting properties meet minimal qualifications and certification requirements to perform inspections, which ensure that those properties are safe, decent, sanitary, and good repair.[15]

[14] Audit Report 2018-CF-0801, HUD Did Not Provide Acceptable Oversight of the Physical Condition of Residential Care Facilities, issued January 5, 2018
[15] Audit Report 2018-FW-0003, REAC Could Improve Its Inspections Processes and Controls, issued August 31, 2018

TOP MANAGEMENT CHALLENGE

2

Protecting the FHA Mortgage Insurance Fund

- A Lack of Sufficient Safeguards in FHA's Mortgage Insurance Program
- Large Losses to FHA's MMI Fund Due to HECM
- Increase in Ginnie Mae's Nonbank Issuer Base
- Potential Emerging Risks Related to a Market Shift Toward an Entirely Digital Mortgage Life Cycle

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HUD, through the Federal Housing Administration (FHA), insures approximately 25 percent of all mortgages in the United States. Using the Mutual Mortgage Insurance fund (MMI),[16] FHA insures lenders against losses when borrowers default on loans, which allows lenders to make loans to individuals who might otherwise not be eligible for a conventional mortgage. As of June 2018, FHA insured a portfolio of more than 8 million mortgages with an outstanding principal balance of nearly $1.2 trillion. From April 2017 through March 2018, the MMI fund paid out almost $14 billion. For those claims for which the lender conveyed the property to HUD and HUD resold the property, HUD recovered only about 54 percent of the funds paid out.

The Government National Mortgage Association (Ginnie Mae) is a self-financing, wholly owned U.S. Government corporation within HUD. It is focused on providing investors a guarantee backed by the full faith and credit of the United States for the timely payment of principal and interest on mortgage-backed securities (MBS) secured by pools of government home loans, which are insured or guaranteed by (1) FHA, (2) HUD's Office of Public and Indian Housing (PIH), and other Federal Government loan programs. The purchasing, packaging, and reselling of mortgages in a security form frees up funds used

[16] The MMI fund is a Federal fund that insures mortgages guaranteed by FHA. The MMI fund supports both FHA mortgages used to buy homes and reverse mortgages used by seniors to extract equity from their homes.

by lenders to provide more loans. Ginnie Mae has an outstanding portfolio of MBS securities valued at $2 trillion and outstanding MBS commitments of $128 billion.

HUD is challenged in protecting the FHA mortgage insurance program. Without sufficient controls, oversight, and effective rules, FHA's MMI fund is at risk of unnecessary losses. Further, if insurance fees collected from borrowers cannot support the fund, additional funding from the U.S. Department of the Treasury is required, as authorized for Federal credit programs. HUD is also challenged by the significant increase in the number of nonbanks issuing MBS pools that are guaranteed by Ginnie Mae.

In protecting the FHA and Ginnie Mae programs, HUD is confronted with

1. a lack of sufficient safeguards in FHA's mortgage insurance program,
2. large losses to the insurance fund due to home equity conversion mortgages (HECM),
3. an increase in Ginnie Mae's nonbank issuers, and
4. potential emerging risks related to a market shift toward an entirely digital mortgage life cycle.

A Lack of Sufficient Safeguards in FHA's Mortgage Insurance Program

In 2008, as a result of the financial crisis, FHA lenders became one of the main mortgage lenders in the single-family mortgage market. With the resulting increased market share, the FHA MMI fund faced greater risk. FHA has failed to develop sufficient safeguards to protect the MMI fund from this increased risk.

One example is that FHA failed to create safeguards, which would prevent loan servicers that do not meet foreclosure and conveyance deadlines from incurring excessive holding costs. These costs are then transferred to HUD and reimbursed to the servicers as part of the insurance claim on the defaulted mortgage.

In October of 2016, we projected that HUD paid claims for nearly 239,000 properties that servicers did not foreclose upon or convey on time. As a result, HUD paid an estimated $2.23 billion in unreasonable and unnecessary holding costs over a 5-year period.

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These excessive costs were allowed to occur because HUD regulations do not establish a maximum period for filing a claim and do not place limitations on holding costs when servicers do not meet all deadlines. HUD previously started the rulemaking process to address these issues but withdrew its efforts based on concern from mortgage servicers.

If HUD does not pursue changes to FHA program regulations, these excessive costs will continue to negatively affect the MMI fund.[17]

Additionally, FHA lacks sufficient safeguards to prevent it from improperly insuring single-family loans. For example, we identified ineligible loans made to borrowers with delinquent Federal debt or who were subject to Federal administrative offset for delinquent child support. In calendar year 2016 alone, we estimate that FHA, through its approved lenders, insured more than 9,500 ineligible loans worth $1.9 billion.[18] As a result, the MMI fund faces a higher risk of loss.

Large Losses to FHA's MMI Fund Due to HECMs

HECM is a reverse mortgage program that enables elderly homeowners to borrow funds using the equity in their homes. In HUD's 2017 Annual Report to Congress[19] regarding the financial status of the MMI fund, HUD reported that the reverse mortgage program continued to have a negative impact on the fund. The report cited that the HECM portfolio had a capital ratio of *negative* 19.84 percent and an economic net worth of *negative* $14.5 billion. This declaration by HUD is compelling, largely because HECM origination volume has trended up for most of the past 20 years. This trend would indicate that the negative performance would accelerate as the larger volumes mature.

The reverse mortgage program is complicated and ripe for a host of fraud schemes due to the program intricacies and implementation. Updating its rules and policies would help reduce some of the inherent issues. For example, housing counseling is required to obtain the loan, but HUD does not require that these sessions be conducted in person. A great majority of these counseling sessions take place over the telephone. A housing counselor would not know whether he or she was speaking with the borrower or someone posing as the borrower or whether an interested party or family member was coaching the elderly borrower. From a 2016 report by the National Center on Elder Abuse, almost 58 percent of people who take advantage of older adults' finances are family members.[20]

Further, a property's home value is one of the key factors in determining the amount allowed for the loan. To ensure that the home is valued accurately, it is important to verify that appraisers are independent and have no financial interest in the transaction. We have reported instances of fraudulent appraisals being used to increase HECM loan amounts to qualify senior borrowers for larger HECM loans. Our investigations have revealed HECM appraisals in which appraisers claim that the property values have increased by 60 to 100 percent, while other properties in the same area are appreciating only 3 to 4 percent.[21]

To help address this issue, on September 28, 2018, FHA released Mortgagee Letter 2018-06, which requires a second appraisal for certain HECMs. Given the volatility in the HECM program and its disproportionate effect on the MMI fund, FHA has decided to

[17] Single-Family Mortgage Insurance Claims, 2017-KC-0001, issued October 14, 2016
[18] Audit Report 2018-KC-0001, FHA Insured $1.9 Billion in Loans to Borrowers Barred by Federal Requirements, issued March 26, 2018
[19] Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund, Fiscal Year 2017, published November 15, 2017: https://www.hud.gov/sites/dfiles/CFO/documents/2017fhaannualreport.pdf
[20] Elder Abuse Awareness Day Spotlights Reverse Mortgage Consumer Protections," June 15, 2016, by Alana Stramowski
[21] Industry Alert: Reverse Mortgage Refinancing, November 30, 2015

require that higher risk HECMs undertake a second appraisal to ensure credibility in assessing the collateral risk. In situations in which there is a second appraisal, the lower value appraisal is to be used in originating the loan.

In addition to fraudulent appraisals, we have seen that delayed claim reporting by the servicers or financial institutions adds many additional costs to the HECM claim, which the MMI fund ultimately must pay. These costs could be mitigated by closer oversight of claims and lenders' compliance with self-curtailment rules.

Increase in Ginnie Mae's Nonbank Issuer Base

Ginnie Mae's business has increasingly relied on nonbanks, which now represent most annual security issuances. Nonbanks are financial institutions that offer only mortgage-related services. Nonbanks serving as Ginnie Mae issuers take full responsibility for servicing, remitting, and reporting activities for the mortgages in each of their pools. In fiscal year 2016, nonbank issuers accounted for 73 percent of Ginnie Mae's single-family MBS issuance volume for the year, up from 51 percent in June 2014 and from 18 percent in fiscal year 2010. As we and Ginnie Mae have reported, the increase in the number of nonbank issuers and their complexity continues to present an unmitigated challenge for monitoring efforts.[22]

In a September 2017 audit, we found that Ginnie Mae was not prepared for the rapid growth and shift from banks to nonbanks in its issuer base and its staff lacked the skills necessary to immediately respond to increased risks posed by these changes. As a result, Ginnie Mae may not identify problems with issuers in time to prevent a default. A default would occur if the issuer did not pay investors in a timely manner. Additionally, Ginnie Mae may not be able to properly service mortgages absorbed in a default and may require additional funds from the U.S. Treasury to pay investors if a large issuer default occurs.[23]

We had also identified shortcomings in Ginnie Mae's issuer default governance framework when conducting Ginnie Mae's fiscal year 2016 financial statement audit. At that time, Ginnie Mae lacked a formal process and protocol to establish this framework, which could lead to failing to properly capture the loss contingencies measured under the MBS program guaranty financial statement line item. This framework includes the identification, monitoring, analysis, evaluation, and response to potential issuer defaults. As part of its corrective action plans to address issuer defaults, Ginnie Mae is developing the Default Playbook, which attempts to create a new framework to address issuer default management. During fiscal year 2018, significant strides were made in improving and operationalizing the playbook; however, it is an ongoing project with an expected completion date of September 30, 2019.

[22] OIG Topic Brief, Monitoring of Nonbank Issuers, February 28, 2017
[23] Audit Report 2017-KC-0008, Ginnie Mae Did Not Adequately Respond to Changes in Its Issuer Base, issued September 21, 2017

Potential Emerging Risks Related to a Market Shift Toward an Entirely Digital Mortgage Life Cycle

The mortgage industry is moving toward an entirely electronic loan process. FHA and Ginnie Mae intend to do the same. However, HUD, particularly FHA, has well-known technology challenges as described later in this document. Adding new platforms and security measures required for digital mortgages presents potentially significant risks to the agency, industry, and consumer. Risks include information security, data transfers and platform integration, and system functionality, all of which could lead to fraudulent activities.

TOP MANAGEMENT CHALLENGE

3

Providing Adequate Monitoring and Oversight of its Operations and Program Participants

- Insufficient Monitoring of Its Operations
- Monitoring and Oversight of Its Programs and Program Participants

HUD continues to struggle with effective oversight controls, which in turn impacts its ability to monitor its operations and program participants. About $48.2 billion a year passes through HUD to State and local governments, organizations, and individuals in the form of grants, subsidies, and other payments. HUD's work is critical to strengthening these communities, bolstering the economy, and improving individuals' quality of life. However, HUD continues to face challenges with effective program management of the nearly $50 billion in Federal funds targeted for these individuals and entities. For example, in fiscal year 2018, our reports identified more than $1.3 billion in questioned costs[24] and nearly $4.7 billion in funds put to better use.[25] As stated earlier in the introduction of this document, HUD's personnel levels have declined significantly over time. This situation has impacted its ability to sufficiently monitor and oversee its operations and program recipients.

[24] Questioned costs - Costs that have been challenged during the audit by the auditor and are comprised of three categories of costs: ineligible costs, unsupported costs, and unnecessary or unreasonable costs.

[25] Funds put to better use – Funds to be put to better use quantify monetary savings from management actions, in response to OIG recommendations, which prevent improper obligations or expenditures of agency funds or avoid unnecessary expenditures.

Insufficient Monitoring of its Operations

For many years, we have reported on HUD's lack of compliance with GAO's internal control standards. GAO's Standards for Internal Control in Federal Government provide the framework for, in part, establishing and maintaining internal control, known as management control.[26]

HUD's handbook that establishes HUD's management control program to comply with provisions of significant laws and regulations implemented the requirement for management control reviews (MCR).[27] The handbook details the roles and responsibilities of individual program offices regarding the internal controls over HUD programs and administrative functions. It also details key processes – including MCRs – which each program office must follow to provide reasonable assurance that programs and activities are effectively and efficiently managed and are protected against fraud, waste, abuse, and mismanagement.

Beginning in 2015, we reported that HUD was not conducting routine or timely MCRs and could not ensure that its programs were operating as intended. In fiscal year 2016, GAO cited governance weaknesses specifically related to HUD's inconsistent performance of key departmental monitoring controls, such as program evaluations that evaluate the effectiveness of a program.

In fiscal year 2017, we found that HUD did not conduct any routine or timely MCRs for its programs as required by HUD guidance. The HUD handbook that establishes HUD's management control program has been under revision for more than a year, prolonging the absence of guidance required for these reviews.

In fiscal year 2017, we found that HUD did not conduct any routine or timely MCRs for its programs as required by HUD guidance.[28] The HUD handbook that establishes HUD's management control program has been under revision for more than a year, prolonging the absence of guidance required for these reviews.

Inconsistent performance of MCRs deprives management of an important monitoring tool that should provide key feedback on the effectiveness and efficiency of departmental operations.[29]

Efforts to implement associated recommendations offered by OIG or GAO have been halted due to unclear responsibility for the management control program between the Office of the Chief Financial Officer (OCFO) and the Office of Strategic Planning and Management. Therefore, MCRs have not improved in consistency, frequency, or timeliness.

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[26] GAO-14-704G, issued September 10, 2014

[27] An MCR is a detailed evaluation of the complete system of management controls in a functional area.

[28] HUD Handbook 1840.1

[29] Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S. Department of Housing and Urban Development Financial Audit, 2018-FO-0004, issued November 15, 2017; Additional Details To Supplement Our Fiscal Years 2016 and 2015 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit 2017-FO-0003, issued November 15, 2016; Additional Details To Supplement Our Fiscal Years 2015 and 2014 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit 2016-FO-0003, issued November 18, 2015

Monitoring and Oversight of its Programs and Program Participants

Over time, we have demonstrated that HUD's lack of sufficient monitoring limits its ability to prevent and detect fraud, waste, and mismanagement. Specifically, grantees and PHAs have not been able to support or have misspent millions of dollars, with little risk of detection or suffering repercussions for mismanagement of the funds. In addition, HUD's monitoring did not always identify and address the root causes of residential care facilities' financial or operational challenges.

Monitoring of Grantees:

Approximately 16 percent of HUD's annual appropriations are provided as grants through its Office of Community Planning and Development (CPD) in its charge to develop viable communities by promoting integrated approaches that provide decent housing and a suitable living environment and expand economic opportunities for low- and moderate-income persons. To achieve these goals, CPD relies upon partnerships with all levels of government and the private sector. Grant recipients in turn often use subgrantees, other government agencies, and private-sector companies to help them accomplish their objectives.

In fiscal years 2014 through 2017, at least 21 of our audits of CPD programs have found little or no monitoring of the grantees. In 2017,[30] we found challenges with the field office risk assessment process. We found that field office staff did not follow CPD risk assessment and monitoring requirements and field office management responsible for reviewing staff performance did not correct the noncompliance of staff members performing these functions. In addition, the headquarters desk officer review function was administrative in focus and failed to note noncompliance. Therefore, we determined that CPD could not be assured that its field offices correctly identified high-risk grantees or conducted adequate monitoring to mitigate risk to the integrity of CPD programs. Consequently, in 2018,[31] we performed a comprehensive review of CPD's monitoring and reported that its risk assessment and monitoring did not provide effective oversight of programs and grantees. CPD headquarters did not have effective supervisory controls and structured the risk assessment and monitoring model so that CPD field office directors would have substantial responsibility for ensuring the accuracy and effectiveness of the model. CPD headquarters' responsibility for the model was limited to the design and general policy development, along with administrative matters. As a result, CPD did not have assurance that it correctly assessed grantee risk, prepared accurate work plans, or monitored grantees in compliance with requirements. Accordingly, CPD could not have confidence regarding accuracy, validity, or conclusions drawn.

In its 2019 congressional budget justification,[32] CPD stated that it monitored only 13 percent of the grantees in its portfolio. Given the extent of findings uncovered in our grantee audits, limited monitoring hinders HUD in identifying poorly performing grantees. The challenge for CPD is the growing inventory of open grants caused by the annual award of multiyear grants, more disaster grants, and the backlog of grant closings.

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[30] Audit Report 2017-FW-0001, HUD's Office of Community Planning and Development Did Not Appropriately Assess State CDBG Grantees' Risk to the Integrity of CPD Programs or Adequately Monitor Its Grantees, issued July 10, 2017
[31] Audit Report 2018-FW-0001, CPD's Risk Assessment and Monitoring Program Did Not Provide Effective Oversight of Federal Funds, issued June 26, 2018
[32] HUD 2017 congressional budget justification, accessed https://www.hud.gov/sites/documents/FY_2017_CJS_COMBINED.PDF

CPD's staffing and travel budgets continue to decrease, making new risk-based strategies imperative. While CPD is trying to increase its oversight through remote monitoring, its effectiveness will continue to be hampered by the reliability of the information and level of detail it receives from the grantee.

During our 2014 annual financial statement audit, we discovered that CPD had waived the Office of Management and Budget (OMB) requirement for its grantees to complete the Federal Financial Report, Standard Form (SF) 425.[33] When questioned, CPD acknowledged that this practice had been ongoing for some time and continued. The SF-425 report captures information regarding the obligations and disbursements that occurred during the grant period and the program income earned as a result of work performed as part of the grant agreement. If obtained, this information would provide CPD a window to the financial status of each open grant award. This would assist CPD to determine whether grantees complied with applicable regulations and statutes, thus strengthening its monitoring and oversight of grantees. The data also provides valuable financial information that OCFO can use to perform financial management and accounting analyses to ensure accurate financial reporting of HUD's programs. Data collected from this form could have been used to address major financial reporting weaknesses that have contributed to HUD's disclaimer of opinion on its consolidated financial statements for the last 5 years.

Monitoring of PHAs:

The role of PIH is to ensure safe, decent, sanitary, and affordable housing; create opportunities for residents' self-sufficiency and economic independence; and assure fiscal integrity by all program participants. Approximately 35.3 percent of HUD's annual appropriations flow through PIH. A large portion of PIH funding is spent on its Housing Choice Voucher Program, which is administered by PHAs. HUD electronically monitors the voucher program through a system that is reliant upon PHAs' self-assessments and self-reported information. Past audits and HUD's onsite reviews have confirmed that self-assessments are not always accurate, causing us to question the reliability of the information in PIH systems. Due to its limited funding for new systems development and staffing constraints, PIH employs a risk-based approach to monitoring. Currently, HUD uses a Two-Year Tool to analyze a PHA's utilization situation and a National Risk Assessment Tool to determine which PHAs need increased monitoring or technical assistance, based on their performance, amount of funding, and compliance scores. HUD will continue to face challenges in monitoring this program until it has fully implemented a reliable, real-time, and all-inclusive monitoring tool.

In an attempt to streamline activities to provide relief to PHAs, PIH allowed PHAs to use a fee-for-service model to pay a central office cost center for certain costs rather than allocating overhead costs. This practice affects Housing Choice Voucher, Public Housing Operating Fund, and Public Housing Capital Fund program funds. Once paid to the central office cost center, the funds are defederalized, meaning they are no longer required to be spent on the respective PIH programs. Past audits questioned HUD's lack of support for its central office cost center fee limits and found that PHAs transferred ineligible and unsupported funds to the central office cost centers. In response, HUD started the rulemaking process so program funds paid to the central office cost center

[33] OMB Standard Form 425 – Federal Financial Report, to track the status of financial data tied to a particular Federal grant award. See the top management challenges on monitoring and oversight and financial management system weaknesses for additional information.

would maintain their status as Federal funds. HUD also agreed to assess the reasonableness of the central office cost center fee limits regularly.

Additionally, we reported that HUD lacked adequate justification for allowing PHAs to charge an asset management fee, resulting in more than $81 million in operating funds being unnecessarily defederalized annually. HUD has not yet corrected this issue. Therefore, we continue to have concerns about the fee's necessity. However, our concerns should be mitigated when HUD implements the rule federalizing the amounts and restricting their use.[34]

Monitoring of Section 232 Residential Care Facilities:

FHA provides mortgage insurance for residential care facilities, such as nursing homes, assisted living facilities, and board and care homes. Insurance can cover the purchase, refinance, new construction, or substantial rehabilitation of a project. In a recent audit, we found that HUD's monitoring was not effective in addressing problems at 18 financially challenged nursing homes reviewed.

As a result, HUD could lose more than $32.1 million for four defaulted mortgages, and HUD owed more than $10 million in carrying costs to the respective lenders and lost more than $9.7 million in a bankruptcy sale.

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Additionally, HUD did not take action on ineligible expenses of more than $7.8 million, unsupported expenses of more than $8.9 million, and accrued expenses of more than $44.4 million.[35]

We also issued a management alert[36] to the Office of Healthcare Programs. We found that HUD failed to provide oversight of the physical condition of the residential care facilities in its portfolio to ensure that owners maintained the value of the properties for the life of the HUD-insured mortgage. We consistently saw the same types of deficiencies recurring throughout the facilities we visited. These deficiencies included significant roof problems that caused leaks and water damage, poor quality of repairs performed by unskilled labor, and facilities that were neglected and generally run down. The REAC inspections we reviewed with scores below 31 (out of 100) were performed an average of almost 3 years apart. In addition, the REAC scores did not always accurately reflect the overall physical condition of the facilities. These deficiencies are indications of a lack of physical condition monitoring by HUD and a lack of concern for the structural quality of the collateral by the owners and operators.

[34] Audit Report 2014-LA-0004, HUD Could Not Support the Reasonableness of the Operating and Capital Fund Programs' Fees and Did Not Adequately Monitor Central Office Cost Centers, issued June 30, 2014
[35] Audit Report 2018-BO-0001, HUD's Office of Residential Care Facilities Did Not Always Have and Use Financial Information to Adequately Assess and Monitory Nursing Homes, issued September 17, 2018
[36] Management Alert - HUD Did Not Provide Acceptable Oversight of the Physical Condition of Residential Care Facilities, 2018-CF-0801, issued January 5, 2018

TOP MANAGEMENT CHALLENGE

4

Administering Disaster Recovery Assistance

- Codifying the CDBG-DR Program
- Ensuring That Expenditures Are Eligible and Supported
- Ensuring and Certifying That Grantees Are Following Federal Procurement Regulations
- Addressing Concerns That Citizens Encounter When Seeking Disaster Recovery Assistance
- Preventing Fraud in Disaster Recovery Assistance

HUD plays a substantial role in national disaster recovery initiatives. HUD often receives more disaster recovery funding than any other Federal entity. Congress has appropriated more than $84.6 billion in supplemental funding to HUD for disaster recovery since 2001. This amount includes $35.8 billion appropriated by Congress in supplemental appropriations to HUD in 2017 and 2018 for recovery from Hurricanes Harvey in Texas; Irma in Florida, Georgia, South Carolina, and the U.S. Virgin Islands; Maria in Puerto Rico and the Virgin Islands; and Nate in Mississippi. These disasters resulted in the loss of many human lives and massive property destruction.

HUD's primary program for disaster recovery assistance is Community Development Block Grant Disaster Recovery (CDBG-DR) program. Through the CDBG-DR program, HUD awards grants to States and units of local government for disaster recovery efforts. The nature of disaster recovery is inherently risky and susceptible to fraud, given the complexity and range of challenges experienced when recovering from disasters. Disaster recovery appropriation funds may take decades to spend, as their purpose is for long-term recovery, which includes rebuilding homes and communities. Over the years, HUD has gained more experience and made progress in assisting communities recovering from disasters, but it continues to face the following challenges in administering and overseeing these grants:

- codifying the CDBG-DR program,
- ensuring that expenditures are eligible and supported,
- ensuring and certifying that grantees are following Federal procurement regulations,
- addressing concerns that citizens encounter when seeking disaster recovery assistance, and
- preventing fraud in disaster recovery assistance.[37]

Codifying the CDBG-DR Program

When HUD initiated CDBG-DR assistance, it did not establish a formal CDBG-DR program in the Code of Federal Regulations. Instead, it has routinely issued multiple requirements and waivers for each disaster recovery supplemental appropriation in Federal Register notices, many of which have been repeated from disaster to disaster. In a recent report, HUD's Office of Block Grant Assistance (OBGA) stated that it had not codified the program because it believed it did not have the authority or had not determined its authority under relevant legislation.[38] It also believed a Presidential Executive order presented a barrier to codification, as it required CPD to identify two rules to eliminate before creating a new codified rule. We believe OBGA has the authority under the Housing Act of 1974 and it should codify the program. OBGA's use of multiple Federal Register notices to operate the CDBG-DR program presented challenges to the grantees. For example, 59 grantees with 112 active CDBG-DR grants totaling more than $47.4 billion as of September 2017 had to follow requirements contained in 61 different Federal Register notices to manage the program. Codifying the CDBG-DR program would (1) ensure that a permanent framework is in place for future disasters, (2) reduce the volume of Federal Register notices, (3) standardize the rules for all grantees, and (4) ensure that grants are closed in a timely manner.[39]

Ensuring That Expenditures Are Eligible and Supported

Most CDBG-DR funding is available until spent, except for Hurricane Sandy funding, which had to be obligated by the end of fiscal year 2017. Of the $84.6 billion appropriated by Congress for various disasters since 2001, $65.67 billion (80.1 percent) had been obligated, and $38.98 billion (45 percent) had been disbursed as of September 30, 2018. While disbursing disaster recovery appropriations takes time, in some cases, many years have passed since the specific disaster occurred, and significant disaster funds remain unspent. HUD's challenge has been ensuring that grantees have the capacity to administer the funds and are using disbursed disaster funds for eligible and supported items.

[37] Helen M. Albert, Acting Inspector General: Testimony before the United States House of Representatives Committee on Financial Services Subcommittee on Oversight and Investigations Reforming the Community Development Block Grant-Disaster Recovery Program, November 1, 2017. Accessed at https://www.hudoig.gov/sites/default/files/Albert%20Testimony.pdf

[38] HUD did not believe it have the authority to codify CDBG-DR under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, and it had not determined whether it had the authority under the Housing and Community Development Act of 1974 as amended.

[39] Audit Report 2018-FW-0002, HUD's Office of Block Grant Assistance Had Not Codified the Community Development Block Grant Disaster Recovery Program, issued July 23, 2018

We have dedicated substantial effort gaining an understanding to the challenges inherent in HUD's administration and oversight of disaster recovery funding and making recommendations to help HUD better serve populations in need as a result of disasters.

Since 2006, we have completed 120 audits and 6 evaluations relating to CDBG-DR funding for 9-11, Hurricanes Katrina, Sandy, and other eligible disasters. From this work alone, we identified more than $477.4 million in ineligible costs, $906.5 million in unsupported costs, and $5.5 billion in funds that could be put to better use. Additionally, we initiated 649 criminal investigations related to Hurricanes Katrina and Sandy. Lessons learned from administering funds for past disasters provide valuable insight in the response to disaster appropriations related to HUD's administration of the $35.8 billion provided in 2017 and 2018.

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Because HUD disaster relief assistance may fund many recovery activities, HUD helps communities and neighborhoods that otherwise might not recover due to limited resources. However, due to the diverse nature of the projects and the fact that some construction projects may take between 5 and 10 years to complete, oversight of these activities is made more difficult.

The extraordinarily destructive nature of the hurricanes that hit the United States in 2017 present unique challenges for all involved. HUD is in the position of handing over billions of dollars to grantees in Florida, Texas, Puerto Rico, and the U.S. Virgin Islands, which formerly handled, at most, tens of millions of dollars or may have not handled any disaster recovery funds. In addition, Puerto Rico essentially filed for bankruptcy relief, yet is scheduled to receive more than $18 billion in disaster recovery assistance from HUD. Therefore, we have concerns that these entities could have capacity issues in ensuring that the funds are spent appropriately and in a timely manner on disaster recovery activities. Capacity issues, therefore, pose great risks to the successful disbursement of funds in helping citizens and communities recover.

Two audit reports illustrate these challenges for HUD in administering disaster recovery programs. In our review of St. Tammany Parish's Disaster Recovery grant program,[40] we determined that Parish officials did not perform adequate cost analyses, maintain complete procurement files, fully implement a fraud prevention policy, or have an internal audit function. As a result of these systemic deficiencies, the Parish could not reasonably

[40] Audit Report 2017-FW-1004, St. Tammany Parish, Mandeville, LA, Did Not Always Administer Its CDBG Disaster Recovery Grant in Accordance With HUD Requirements or as Certified, issued April 6, 2017

assure HUD that it would properly administer, adequately safeguard, and spend its remaining $8.67 million allocated for CDBG-DR funds in accordance with requirements and paid more than $400,000 in questioned costs. In our review of the State of Connecticut's management of its Sandy CDBG-DR grants,[41] we found that the State did not always comply with the requirements for its owner-occupied rehabilitation and reimbursement programs. Specific issues included improper procurements, inadequate environmental reviews, and an unsupported national objective.[42] As a result, more than $2.4 million in CDBG-DR funds was ineligible, and more than $13.5 million was unsupported.

Ensuring and Certifying That Grantees Are Following Federal Procurement Regulations

We also continue to have concerns about HUD's ability to ensure that disaster recovery grantees are following Federal procurement regulations. After HUD implemented actions to correct procurement issues identified in a 2013 audit report,[43] we completed a rollup report in September 2017,[44] summarizing new issues from 17 subsequent audit reports on disaster recovery grantees with questioned costs totaling nearly $391.7 million, related to procurement. The additional issues came about as a result of HUD's allowing States to certify to requirements using their own standards rather than regulating each aspect of the program.[45] In two other recent audits, we found that HUD could not always provide accurate and supported certifications of State disaster recovery grantee procurement processes[46] or require State grantees to have procurement standards that aligned with each of the Federal procurement standards. As a result, products and services may not have been purchased competitively at fair and reasonable prices.[47]

Addressing Concerns That Citizens Encounter When Seeking Disaster Recovery Assistance

Individuals face challenges in attempting to receive assistance from HUD or any of the Federal and State agencies, nonprofits, or others offering assistance to those affected by a disaster, which often reduce the potential impact of available funding and resources. According to a recent OIG evaluation, citizens may face a circuitous path to receiving disaster recovery assistance, depending on how, when, and where they enter the response effort. Many nonprofit, private, and government organizations and agencies provide citizens – homeowners and businesses – a range of assistance and access in

[41]Audit Report 2017-BO-1001, The State of Connecticut, Community Development Block Grant Disaster Recovery Assistance Funds, issued October 12, 2016
[42] National objectives are requirements of the CDBG program that grantees must meet, including benefiting low- and moderate-income persons, preventing or eliminating slums or blight, and meeting urgent needs.
[43] Audit Report 2013-FW-0001, Generally, HUD's Hurricane Disaster Recovery Program Assisted the Gulf Coast States' Recovery; However, Some Program improvements Are Needed, issued March 28, 2013
[44] Audit Report 2017-PH-0002, HUD Did Not Provide Sufficient Guidance and Oversight To Ensure That State Disaster Grantees Followed Proficient Procurement Processes, issued September 22, 2017
[45] HUD refers to this practice as "maximum feasible deference."
[46] Audit Report 2016-PH-0005, HUD Certifications of State Disaster Grantee Procurement Processes, issued September 29, 2016
[47] Audit Report 2017-PH-0002, HUD Did Not Provide Sufficient Guidance and Oversight To Ensure That State Disaster Grantees Followed Proficient Procurement Processes, issued September 22, 2017

the disaster response and recovery process. The path is not linear, and citizens may start at various points within the disaster recovery assistance process. Citizens may experience lengthy delays from the initial application process to the closing of their cases due to inconsistent communication, coordination, and collaboration. Further, citizens may experience delays in funding, duplication of benefits, and other challenges after the process.[48]

Preventing Fraud in Disaster Recovery Assistance

Another challenge to HUD has been how to provide assistance in an expedited manner while also maintaining adequate safeguards to deter and detect fraud. Working with partners across the Federal Government and Inspector General community, we have identified common fraud schemes and leveraged data analytics in trying to prevent their recurrence. Disaster recovery fraud not only unlawfully enriches the individual submitting the fraudulent application for aid, but also limits the aid that is available to go to those with legitimate needs. Our investigations have identified unscrupulous contractors and individuals who preyed on a public eager to rebuild devastated areas, taking advantage of and further traumatizing the intended recipients. Many schemes involved homeowners who were affected by the disaster but were not eligible for the aid. The following are the most prevalent fraud scheme types identified by investigators during previous disasters that have resulted in indictments, convictions, and recoveries:

- Homeowners fraudulently identifying a second home or an investment property as their primary residence
- Homeowners falsely purporting damage to properties that did not sustain damage during the disaster
- Landlords collecting dual payments from HUD- and FEMA-subsidized rental assistance programs
- Sale of a rental property before the receipt of the homeowner rental assistance grant
- Homeowners receiving grants for properties they did not own
- Restoration contractors defrauding the public by not completing contracted work
- Public corruption connected to State and local officials and contractors

[48] Evaluations Report 2017-OE-0002S, Navigating the Disaster Assistance Process, issued April 10, 2017

TOP MANAGEMENT CHALLENGE

5

Modernizing Technology and the Management and Oversight of Information Technology

- IT Modernization
- IT Procurement
- Project Management

HUD has recently made efforts to modernize its information technology (IT) infrastructure and continues to attempt to address some of its outstanding IT and cybersecurity challenges. However, HUD's ability to effectively manage and oversee its key programs is greatly hindered due to HUD's struggle to resolve persistent IT management challenges. Further, IT system vulnerabilities that could lead to data breaches exist within the HUD IT environment, and HUD has demonstrated an inability to incorporate federally mandated requirements[49] and key practices[50] into effective operational management.

On August 14, 2018, Secretary Carson announced that the position of Chief Information Officer (CIO) would report directly to him. He also directed that the IT functions dispersed across the agency be consolidated into the Office of the Chief Information Officer (OCIO), rather than being held separately by each program office. Further, after this reorganization, the CIO will establish knowledge and skills standards for all agency IT personnel and identify positions in which critical hiring needs exist or there is a shortage of highly qualified candidates and use special hiring authorities to address these staffing risks. For these changes to be effective, HUD must continue to pursue its planned changes and their implementation.

HUD struggles to remain compliant with Federal requirements and to address its IT challenges. Since 2007, we have issued a number of reports related to HUD IT issues

[49] Federal mandated requirements include OMB, U.S. Department of Homeland Security, and Executive order directives and memorandums requiring implementation of cybersecurity program enhancements.
[50] Key practices are strategies and recommendations for improving cybersecurity programs that often come from the National Institute of Standards and Technology, Federal agencies, and vendors.

with more than 483 recommendations to help HUD address these challenges. Of these recommendations, 197 remain open or unresolved, with another 25 open recommendations from GAO. HUD OIG and GAO have repeatedly made multiple recommendations because the original recommendations were closed without proper remediation or the issues persisted without being addressed.

IT Modernization

HUD continues to manage most of its operations with legacy systems implemented between 1974 and 1995. Many of HUD's legacy systems are outdated and cannot be adapted to handle the increasingly complex tasks required for HUD's mission in the 21st century. HUD's aging technology and the reliance on applications that are no longer supported by vendors places HUD's IT systems at an increasing risk of failure and exploitation because critical updates to fix vulnerabilities are often no longer available. This situation increases the risk of possible HUD data breaches. For example, we have reported on weaknesses in internal information system data processing controls and security. The effect of these weaknesses is that the completeness, accuracy, and security of HUD information is at risk of unauthorized access and modification. We are specifically concerned about the current state of FHA's IT systems and the lack of systems capabilities and automation to respond to changes in business processes and the IT operating environment.

As another example of the detrimental effect of outdated systems, we reported in 2017[51] that HUD did not report complete and accurate data to the public as required by the Digital Accountability and Transparency Act of 2014 (DATA Act).[52] The DATA Act expanded prior Federal transparency regulations by disclosing Federal agency expenditures and linking Federal contract, loan, and grant spending information to enable taxpayers and policy makers to track Federal spending. HUD did not follow required data standards meant to ensure the reporting of reliable, consistent Federal spending data for public use because HUD's existing systems did not have the capabilities of implementing these standards. As a result, HUD underreported $17.9 billion in incurred obligations, $16.9 billion in outlays, and $4.2 billion in apportionments. Therefore, stakeholders and end users accessing HUD data provided to the public in response to DATA Act requirements could not obtain a complete and accurate representation of HUD's financial position and performance.

Additionally, maintenance of all HUD legacy systems is very costly due to the specialized skills and support needed to maintain and operate them. HUD's fragmented approach to adopting technology has led to multiple platforms and services competing for resources.

[51] Audit Report 2018-FO-0001, DATA Act Compliance Audit of the U.S. Department of Housing and Urban Development, issued November 3, 2017

[52] Digital Accountability and Transparency Act of 2014, Public Law 113-101, May 9, 2014, https://www.congress.gov/113/plaws/publ101/PLAW-113publ101.pdf

Over the past 5 years, HUD spent between 70 and 95 percent of its, on average, $280 million annual IT budget on operations and maintenance. With each successive year since 2012, HUD has spent less money on development, modernization, and enhancement efforts and, instead, spent more money on operating and maintaining legacy systems.

Over the past 5 years, HUD spent between 70 and 95 percent of its, on average, $280 million annual IT budget on operations and maintenance. With each successive year since 2012, HUD has spent less money on development, modernization, and enhancement efforts and, instead, spent more money on operating and maintaining legacy systems.

From 1991 to 2016, HUD spent approximately $370 million on three IT modernization projects. None of the three was fully completed. In 2016, GAO concluded that turnover among senior leadership, shifting priorities, and resource constraints contributed to HUD's difficulties in implementing needed changes. The lack of proper project management implementation only adds to the challenge of developing and implementing modernization efforts on time and on budget. HUD OCIO was recently awarded an IT modernization grant of $20 million to transition applications from the legacy Unisys mainframe platform to the cloud. Although HUD was recognized for having a detailed modernization proposal for this project, proper oversight will be needed to ensure that information security is built into this and all projects and that tax payers' money is not wasted.

IT Procurement

Contracting officer's representative duties are often performed as additional duties rather than full-time roles. According to the Office of the Chief Procurement Officer, in fiscal year 2017, fewer than five people were adequately trained and possessed the expertise to manage IT projects and contracts. While HUD has adopted many acquisition procedures, it has not fully implemented or applied these procedures, leaving gaps in its IT acquisition framework. GAO reported that HUD lacked well-documented and fully developed selection processes to ensure consistent application of selection criteria used for applicants for contracts.[53] In addition, HUD lacked robust processes for contractor oversight and evaluating contractor performance against expected outcomes to ensure that its contractors met their obligations.

Project Management

HUD program offices generally operate within silos, and the agency has taken a fragmented approach to adopting and implementing technology. HUD recently began an initiative to consolidate IT efforts under OCIO; however, this consolidation has not yet been realized and will take dedicated efforts to achieve. HUD's current decentralized IT

[53] GAO Report, GAO-16-497, Actions Needed to Incorporate Key Practices into Management Functions and Program Oversight, publicly released August 19, 2016

system and application management model has resulted in autonomous applications and duplication of services operating on multiple platforms across program offices. In 2016, we found that three web applications were operating outside HUD's IT environment, showing that OCIO did not have an accurate inventory or knowledge of its web application environment. In 2018, we found an additional web application that was operating outside HUD's IT environment without the knowledge of OCIO. HUD program offices had generally used operational funds to develop IT systems and applications without oversight from OCIO. This shows a lack of progress in IT system implementation and a lack of a consolidated project management capability. As a result, HUD has multiple customized applications to manage its grant programs with no plan to standardize and modernize the grants process and capabilities.

In addition, financial management and IT governance failures led management to disregard or underestimate significant risks. HUD's latest major project implementation, a transition of the financial system to a Federal shared service provider (FSSP) called New Core,[54] failed to meet its stated objectives due to funding shortfalls and constraints, rushed system design and development activities, schedule management deficiencies, and risk management weaknesses. Three years after implementation, HUD is still resolving data conversion issues. Originally, the New Core Project included plans to transition some of HUD's legacy financial systems to new platforms or shared services; however, HUD halted the project in April 2016. No substantial plans exist to modernize the remainder of HUD's financial management systems.[55]

It is imperative that HUD not repeat the mistakes of the past when implementing new projects, especially critical projects such as the transition to the cloud.

[54] In the fall of 2012, the New Core Project was created to move HUD to a new core financial system that would be maintained by a shared service provider, the U.S. Department of the Treasury's Bureau of Fiscal Services.
[55] Audit Report Number 2017-DP-0001, HUD's Transition to a Federal Shared Service Provider Failed To Meet Expectations, issued February 01, 2017; and Audit Report Number 2015-DP-0006, New Core: Release 3 Project Management, issued June 12, 2015.

TOP MANAGEMENT CHALLENGE

6

Instituting Sound Financial Management Governance, Internal Controls, and Systems

- HUD's Financial Management Leadership and Governance
- HUD's Internal Control Framework and Financial Management Maturity
- HUD's Financial Management Systems Weaknesses

Over the last several years, HUD's financial management has been operating at "inadequate" or "basic" levels of maturity[56] due to (1) a weak governance structure, including the lack of a confirmed CFO for a number of years; (2) ineffective internal controls; and (3) an antiquated financial management system consisting of legacy systems and manual processes that have precluded HUD from producing reliable and timely financial reports. As a result, HUD has been unable to achieve an unmodified audit opinion[57] on its financial statements for the last 6 years and has received a disclaimer of opinion for 5 of those years. One of HUDs component entities, Ginnie Mae, has also been unable to achieve an unmodified opinion and has received a disclaimer of opinion for the last 5 years due to poor governance and a weak internal control framework. Ginnie Mae has been unable to appropriately account for and support several financial statement line items in accordance with generally accepted accounting principles, including its nonpooled loan asset portfolio, which totaled as much as $6 billion at one point. HUD's unstable financial management environment weakens public

[56] U.S. Department of the Treasury, Bureau of the Fiscal Service, Federal Financial Management Maturity Model. The Maturity Model is a business tool that helps a CFO self-assess his or her organization's level of financial management discipline, effectiveness, and efficiency. A copy of the model can be found at https://www.fiscal.treasury.gov/fsservices/gov/fit/MaturityModelHandout2017-05-10.pdf.

[57] Codification of Statements on Auditing Standards, AU-C Section 700.11, The opinion expressed by the auditor when the auditor concludes that the financial statements are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

confidence in the government programs HUD administers and prevents HUD's stakeholders from being able to rely upon the Department's financial position.

HUD's Financial Management Leadership and Governance

HUD has had a consistent problem with maintaining strong leadership within OCFO. The CFO position was vacant for 6 of the last 7 years, leaving responsibility for financial management of the agency with the Deputy CFO, who has frequently been in an acting capacity. Similarly, as of September 2018, a number of senior-level positions in Ginnie Mae's OCFO have remained vacant for an extended period. As a result, in 2018, as in previous years, Ginnie Mae relied heavily on contractors for accounting expertise and accepted their advice without being fully evaluated by objective, independent, and well-informed Ginnie Mae executives.

The lack of strong, consistent leadership over an extended period has allowed HUD's internal control environment and framework to weaken, which let deficiencies occur without being detected or prevented and precluded HUD from resolving financial integrity issues in a timely manner.

Programmatic decisions that affected HUD's financial reporting were made without consultation from OCFO, negatively impacting HUD's financial reporting by causing material misstatements or preventing auditability of significant balances.

Programmatic decisions that affected HUD's financial reporting were made without consultation from OCFO, negatively impacting HUD's financial reporting by causing material misstatements or preventing auditability of significant balances.

Many of the material weaknesses, significant deficiencies, and instances of noncompliance with laws and regulations cited in HUD's consolidated financial statement audit reports have existed for several years and may have been resolved more promptly if HUD's leadership had taken immediate action on the recommendations and demonstrated a clear commitment to address the deficiencies. HUD has more than 300 open audit recommendations stemming from the annual consolidated financial statement and Federal Information System Controls Audit Manual audits, many of which are overdue for action.

In January 2018, HUD's CFO was confirmed by the U.S. Senate. Since that time, he has outlined several strategic objectives geared toward bringing HUD's financial management back into a compliant state. Those objectives include development of a comprehensive OCFO transformation strategy, to include (1) improving governance and communication and building relationships across the agency, (2) improving internal controls by evaluating audit findings and developing overall remediation plans and execution, and (3) working with HUD's CIO on an IT strategy to address OCFO data needs. While the objectives and strategy are dynamic and can broadly affect the entire agency, it will require significant financial and human resources commitment from the HUD Secretary, Congress, and other stakeholders and will take multiple years before they can be fully implemented.

HUD's Internal Control Framework and Financial Management Maturity

HUD's processes and financial management integrity are still in the "basic" and "inadequate" stages of the U.S. Treasury's Financial Management Maturity Assessment model due to its disclaimer of opinion, multiple material weaknesses, and heavy reliance on manual processes. HUD's most recent OMB Circular A-123 reviews have cited 19 of 50 financial reporting and complementary internal controls as "failing" or not properly designed.

When HUD transitioned to an FSSP in 2015, OCFO did not ensure that changes in business processes and responsibilities were appropriately documented in policies and procedures. As a result, HUD continues to address problems that occurred as a result of poor implementation planning for its transition to the FSSP.

Ginnie Mae has been working to develop and finalize accounting policies for the last 5 years, which is a first step toward bringing its nonpooled loan asset portfolio into an auditable state. These accounting policies and procedures are still being finalized, and controls over these processes have not been developed, implemented, and executed in an effective and efficient manner.

The weakened internal control framework has allowed errors to occur in HUD's financial reporting, requiring HUD to restate its financial statements for the last 5 consecutive years. In addition, HUD is noncompliant with the DATA Act,[58] the Improper Payments and Elimination and Recovery Act, the Debt Collection Improvement Act, the Federal Financial Management Improvement Act, and the Federal Managers Financial Integrity Act.[59]

During the current year, HUD has been working toward drafting policies, procedures, and other artifacts as part of a broader transformation strategy to improve overall controls across HUD. Improvements to significant financial reporting and accounting processes have been designed and implemented during the last half of the fiscal year. While significant work has been completed and is continuing to address material internal control deficiencies, time is needed to allow for the new processes and controls to mature to a level that can ensure the production of timely and reliable financial reporting, which can be sustained during times of environmental and leadership changes.

HUD's Financial Management Systems Weaknesses

Weaknesses with HUD's financial management systems have been a longstanding, pervasive issue significantly impacting HUD's ability to produce timely and reliable financial reports and comply with significant laws and regulations. As discussed in the technology and data management challenge, HUD continues to operate with many legacy systems and maintains an antiquated infrastructure on which most of the HUD and FHA financial applications reside.

[58] Audit Report 2018-FO-0001, DATA Act Compliance Audit of the U.S. Department of Housing and Urban Development, issued November 3, 2017
[59] Audit Report 2018-FO-0004, Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit, issued November 15, 2017

In an attempt to modernize its financial management systems, in October 2015, HUD transitioned some of its core accounting functions to an FSSP as part of the New Core project. HUD encountered significant challenges with the transition, which impaired the efficiency and effectiveness of HUD's internal controls and operations instead of improving them. For example, inaccurate financial data were included in HUD's general ledger, and data conversion errors occurred, impacting millions of dollars in transactions requiring the processing of a significant number of manual, complex journal entries to perform data cleanup. Additionally, significant differences between the general ledger and subsidiary systems remain unresolved 3 years after implementation. The overall implementation to a shared service provided increased the number of processes required to record financial transactions instead of decreasing them.

Several significant financial business processes continue to be either manual or nonexistent and result in unreliable and untimely financial reporting and poor financial management oversight. For example, Ginnie Mae continues to manually produce stand-alone reports to manage the accounting and processing of activities for its more than $3 billion nonpooled loan assets portfolio. Ginnie Mae and HUD have been working on implementing a financial management system to address this weakness for more than 3 years to bring the nonpooled assets into an auditable state. HUD also continues to perform cash management functions and management of HUD's non-FHA loan guarantee programs using manual Excel spreadsheets or Access databases, preventing OCFO from recognizing all accounting events in its financial records accurately and in a timely manner. Additionally, HUD lacks an adequate cost accounting and property management system to accurately report on the cost of programs and property, plant, and equipment balances. Lastly, the lack of an IT system to collect SF-425 data, such as Federal cash on hand and total disbursements, has prevented OCFO and HUD from obtaining necessary financial information to ensure accurate financial reporting and gaining insight into the financial status of each active grant.

HUD continues to face the challenges associated with maintaining its legacy systems and ensuring that they can support the current housing industry and volume of activity that HUD requires to execute its mission.

Management's Response to the OIG Report on Management and Performance Challenges

HUD is committed to fulfilling its mission to create strong, sustainable, inclusive communities and quality affordable homes for Americans. The work of HUD's OIG helps us to ensure that our programs and employees work to successfully accomplish these goals efficiently and with integrity.

As we continue to shape our relationship with the OIG, we remain steadfast in our commitment to address necessary changes required within HUD and any challenges faced by the communities we support. Specifically, we are focused on improving HUD's infrastructure related to human capital practices, critical internal processes, and our information technologies to further enhance the Secretary's strategic priorities of protecting taxpayer funds and streamlining operations.

These improvements will continue to transform HUD into a more efficient and effective agency and help to ensure the progress made to date provides measurable results. Our organization, in its entirety, is resolute in its charge to collaboratively work with the OIG. We will continue to identify and implement solutions, consistent with our available resources, that will remediate weaknesses, which prevent HUD from obtaining a clean audit opinion.

We are working with the OIG to identify weaknesses that have the largest impact on the disclaimer condition and are focusing our remediation efforts on those areas that we believe will demonstrate management's commitment to sound financial reporting and a strong system of internal controls. HUD agrees that it cannot continue to operate under the shadow of a "Disclaimer of Opinion" and have prioritized the business processes in need of substantive improvement, to further the goal of resolving its longstanding material weaknesses.

Additionally, we will continue to address the challenges in administering programs directed towards victims of natural disasters. The impact of hurricanes and wildfires that continue to occur, will be felt for years to come. We have a fiduciary responsibility to ensure that the funds that the Congress appropriates for HUD to assist the victims of these natural disasters are managed efficiently and effectively so that we can maximize the benefit to those in need.

We appreciate the continued commitment on the part of OIG to provide us with recommendations that will strengthen operations and resolve management challenges.

Top Management Challenges
Facing the U.S. Department of
Housing and Urban Development
in 2019 and Beyond

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