audit report

Issue Date September 30, 2011	
Audit Report Number 2011-FO-0006	

TO: David Sidari, Acting Chief Financial Officer, F

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FROM: Thomas R. McEnanly, Director, Financial Audit Division, GAF

SUBJECT: American Recovery and Reinvestment Act of 2009 Grantees Met Initial Expenditure Requirements, but HUD Should Return Recaptured Funds to the U.S. Treasury and Ensure That Grant Closeout Procedures Comply With the Act

HIGHLIGHTS

What We Audited and Why

We performed an audit of the U.S. Department of Housing and Urban Development's (HUD) compliance with initial expenditure requirements related to six programs funded by the American Recovery and Reinvestment Act of 2009 (ARRA). These HUD programs received more than $8.1 billion of the $13.1 billion in ARRA funding that HUD received. The objectives of our audit were to determine whether (1) HUD grantees complied with their initial expenditure requirements; (2) recaptures were properly recorded and controls over the recapture process existed and complied with the Pay It Back Act; and (3) ARRA funds control plans were appropriately modified to include Pay It Back Act requirements. This audit was conducted in combination with our annual audit of HUD's financial statements.

What We Found

HUD met the initial expenditure requirements for five of the six ARRA programs under review. The remaining program was on track to meet its initial expenditure requirement by its specific expenditure deadline.

However, HUD had $20.85 million in recaptured ARRA funds that must be returned to the U.S. Treasury's general fund. Although $20.85 million in ARRA funds was properly identified for recapture and processed by the Office of the Chief Financial Officer (OCFO), the funds had not been returned to the U.S. Treasury. Additionally, $6.2 million in available funds, which were recaptured before the Pay It Back Act, had not been reallocated and should be sent back to the U.S. Treasury.

We also found that the grant closeout process for two of the six programs may have caused noncompliance with ARRA. The Lead Hazard Reduction program had grant closeout procedures that may have allowed disbursement of funding after the final expenditure deadline. Additionally, Tax Credit Assistance Program (TCAP) grantees had procedures that allowed grantees to retain a percentage of ARRA funds from subgrantees and increased the risk of disbursements made after the expenditure deadline.

Lastly, we found that funds control plans for the selected programs had not been modified to include Pay It Back Act requirements, or modifications had not been reviewed and approved by OCFO.

What We Recommend

We recommend that OCFO immediately return $20.85 million in recaptured ARRA funds to the U.S. Treasury general fund in accordance with the Pay It Back Act. Additionally, we recommend that TCAP immediately recapture $6.2 million in deobligated funds to ensure immediate return to the U.S. Treasury.

Further, we recommend that HUD direct the ARRA program offices to review and, if necessary, revise grant closeout and fund retention policies and procedures to ensure that funds are expended or recaptured in accordance with ARRA requirements.

Finally, we recommend that OCFO review all ARRA funds control plans to determine whether the plans have been appropriately modified and approved to include Pay It Back Act requirements.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided the discussion draft report to HUD on September 15, 2011, and requested a response by September 21, 2011. We received the written response on September 27, 2011. HUD agreed with finding 1 and generally agreed with findings 2, 3, and 4. However, HUD disagreed with some of our recommendations. Specifically, HUD (1) disagreed with the cost classification of $20.85 million in recommendation 2A, (2) requested the recommendations in finding 4 be removed because of existing corrective action plans in place related to the issue, and (3) disagreed with recommendation 3B concerning amending its grant closeout procedures. The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

On February 17, 2009, the American Recovery and Reinvestment Act of 2009 (ARRA)[1] was signed into law and was intended to provide supplemental appropriations for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, and State and local fiscal stabilization. This legislation in total provided $13.1 billion to the U.S. Department of Housing and Urban Development (HUD), of which $8.1 billion was provided for the following six programs: (1) Lead Hazard Reduction program, (2) Homelessness Prevention and Rapid Re-Housing Program (HPRP), (3) HOME Investment Partnerships Program (also known as the Tax Credit Assistance Program), (4) Public Housing Capital Fund formula grants, (5) Public Housing Capital Fund competitive grants, and (6) Native American Housing Block Grant formula grants. The law included specific expenditure and reallocation requirements, which varied by program.

ARRA was amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Title XIII - Pay It Back Act, Sections 1306 and 1613, of Public Law 111-203, enacted on July 21, 2010. The Act amended ARRA to require that funds rejected by the States be rescinded and deposited into the U.S. Treasury general fund. Additionally, it required that funds withdrawn by the head of the executive agency for any reason and unobligated funds that are recaptured be rescinded and returned to the U.S. Treasury general fund by December 31, 2012. The specific expenditure requirements of the six ARRA programs under review are discussed below.

Lead Hazard Reduction

The Lead Hazard Reduction program is composed of the Lead-Based Paint Hazard Control grant program that assists States, Native American tribes, cities, counties or parishes, or other units of local government in identifying and controlling lead-based paint hazards in privately owned rental or owner-occupied housing. ARRA provided funding for the following grant programs: Lead-Based Paint Hazard Control, Lead Hazard Reduction Demonstration, Healthy Homes Demonstration, and Healthy Homes Technical Studies. Grantees must expend 50 percent of the funds within 2 years of the date on which funds became available for obligation and 100 percent within 3 years of such date. The initial expenditure deadline, which varies for each grantee, occurred on April 10, 2011 through May 11, 2011.

Homelessness Prevention and Rapid Re-Housing Program

The Homelessness Prevention Fund provides financial assistance and services to prevent individuals and families from becoming homeless and help those that are experiencing homelessness to be quickly re-housed and stabilized. The funds will provide for assistance to include short-term or medium-term rental assistance, housing relocation, and stabilization services. Grantees must expend 60 percent of the funds within 2 years of the date that funds became available for obligation and 100 percent within 3 years of such date. The initial expenditure deadline, which varies for each grantee, is July 5, 2011 through September 29, 2011.

[1] Public Law No. 111-5, 123 Stat. 115, 224 (2009)

HOME Investment Partnerships Program
The Tax Credit Assistance Program (TCAP) provides grants for capital investments in low-income housing tax credit projects. Funds are provided by a formula-based allocation to the housing credit agencies in each State, which will distribute these funds competitively according to their qualified allocation plan. Grantees must expend 75 percent of the funds within 2 years of ARRA enactment and 100 percent of the funds within 3 years of ARRA enactment. Therefore, the initial expenditure deadline for TCAP grantees is February 17, 2011.

Public Housing Capital Fund
The Public Housing Capital Fund provides funds for the capital and management activities of public housing agencies as authorized under Section 9 of the U.S. Housing Act of 1937. These activities include the modernization and development of public housing. Funds from this program cannot be used for operations or rental assistance. ARRA requires that public housing agencies give priority to capital projects that can award contracts based on bids within 120 days from the date the funds are made available to the agencies. Grantees must expend 60 percent of the funds within 2 years of the date on which funds became available for obligation and 100 percent within 3 years of such date. The initial expenditure deadline for formula grantees is March 17, 2011. The deadline for competitive grantees, which varies for each grantee, is September 8, 2011 through September 22, 2012.

Native American Housing Block Grants
The Native American Housing Block Grant program funds new construction, acquisition, rehabilitation, and infrastructure development activities. Funds can also be used to leverage private-sector financing for new construction, renovation, and energy retrofit investments. Grantees must expend 50 percent of such funds within 2 years of the date on which funds became available for obligation and 100 percent within 3 years of such date. The initial expenditure deadline for formula grantees, which varies for each grantee, is April 14, 2011 through January 19, 2012.

HUD is responsible for ensuring proper control over the funding process. This responsibility lies with the Office of the Chief Financial Officer (OCFO). Below is additional information regarding OCFO's responsibility for the administrative control of funds.

Funds Control Plans
HUD's Administrative Control of Funds Policies and Procedures (CFO Handbook 1830.2, REV-5) states that Congress has vested overall responsibility for establishing an effective administrative control of funds process with the Chief Financial Officer (CFO). Each HUD allotment or suballotment holder is responsible for the proper management and control of all funds allotted to it. Additionally, all allotment holders must prepare a funds control plan describing the administrative control of funds allotted to them. The funds control plan shall be submitted annually for review until the CFO determines that further submission and review are not needed. Once the CFO has determined that further review of a funds control plan is unnecessary, submission of the plan for annual review will not be required unless changes in law, policy, or procedure have occurred that would be inconsistent with the existing plan.

The objectives of our audit were to determine whether (1) HUD grantees complied with their initial expenditure requirements, (2) recaptures were properly recorded and controls over the recapture process existed and complied with the Pay It Back Act and (3) ARRA funds control plans were appropriately modified to include Pay It Back Act requirements,.

RESULTS OF AUDIT

Finding 1: HUD ARRA Programs Were on Target To Meet the Initial ARRA Expenditure Requirements

HUD grantees met ARRA's specific initial expenditure requirements for five of the six ARRA programs reviewed; however, the remaining program did not reach its initial expenditure deadline during the period under review. HUD met the initial expenditure requirements for five of the six programs because the program offices tracked expenditure rates to ensure compliance with ARRA expenditure requirements. As a result, the six programs were in general compliance with ARRA expenditure requirements.

HUD ARRA Programs Were on Target To Meet ARRA Expenditure Requirements

Our review of HUD's ARRA program funding found that the initial expenditure deadline had been reached for five of the six programs reviewed as of May 31, 2011. The remaining program, Public Housing Capital Fund competitive grants, did not reach its initial expenditure deadline during the review. However, it will reach its initial expenditure deadline in the fourth quarter of fiscal year 2011. At the time of our review, the program had substantially[2] met its expenditure requirement.

The programs reviewed, the amount appropriated, the amount awarded or committed, the amount expended, the percentage rate of funds expended, and the expenditure requirements are identified in table I below.

[2] "Substantially" is defined as the program's having met 90 percent or more of the required expenditure rate. The rate for the Public Housing Capital Fund competitive grant is 93.2 percent (55.6 percent divided by 60 percent).

Table I. ARRA expenditures analysis as of May 31, 2011					
ARRA program area	**Appropriated**	**Amount awarded or committed**	**Expenditures**	**Expenditure percentage**	**Expenditure requirements**
HPRP	$1,500,000,000	$1,492,500,000	$956,259,774	64.1%	60% within 2 years of date, 100% within 3 years of date
TCAP	2,250,000,000	2,231,435,074	2,002,702,250	89.7%	75% within 2 years of enactment of ARRA, 100% within 3 years of enactment of ARRA
Public Housing Capital Fund - formula	3,000,000,000	2,979,567,709	2,629,291,133	88.2%	60% within 2 years of date, 100% within 3 years of date
Public Housing Capital Fund - competitive	1,000,000,000	996,430,707	557,104,310	55.9%	60% within 2 years of date, 100% within 3 years of date
Lead Hazard Reduction program	100,000,000	94,985,690	61,967,161	65.2%	50% within 2 years of date, 100% within 3 years of date
Native American Housing Block Grant - formula	255,000,000	251,862,255	221,158,509	87.8%	50% within 2 years of date, 100% within 3 years of date
Total	$8,105,000,000	$8,046,781,435	$6,428,483,136		

The expenditure percentage calculation for five of the six ARRA programs was performed by dividing the amount of expenditures as of May 31, 2011, by the amount awarded as of the same date. The expenditure percentage calculation for the remaining program, TCAP, was based on the amount of funds committed as of May 31, 2011, because ARRA requires that 75 percent of TCAP funds awarded be committed within 2 years of the enactment date of ARRA, which was enacted on February 17, 2009. Therefore, the balance of uncommitted funds was not used to determine the expenditure rate.

Conclusion

HUD met its initial expenditure requirements within the required timeframe for the programs under review, except for the Public Housing Capital Fund competitive grant, which had substantially met its requirement.

Recommendations

There is no formal recommendation, and no further action is necessary.

Finding 2: HUD Did Not Return $20 Million in Recaptured Funds to the U.S. Treasury and Recapture an Additional $6.2 Million in Unobligated TCAP Funds

HUD recaptured $20.85 million in ARRA funds that must be returned to the U.S. Treasury in accordance with the Pay It Back Act. HUD terminated grant agreements and deobligated or recaptured funds for grantees that failed to meet performance or expenditure requirements. However, it had not returned the money because the process for the return of recaptured funds had not been fully implemented. Additionally, HUD deobligated $6.2 million in TCAP funds and had no plans to reallocate the funds. The Office of Community Planning and Development (CPD) program staff deobligated TCAP funds, stated that no plans existed to reallocate and obligate the funds because there were no projects to re-obligate them to, and expected the funds to remain unobligated until the fund expired. Without the timely return of recaptured ARRA funds to the U.S. Treasury, HUD is hindering the spirit of ARRA and the Pay It Back Act and funds cannot be immediately used toward other government programs.

HUD Must Return $20.85 Million in Recaptured Funds to the U.S Treasury

HUD must return $20.85 million in recaptures to the general fund of the U.S. Treasury. Recaptures are current year recoveries of prior year obligations that have not been outlayed. Five of the six programs reviewed had recaptures that were no longer available for obligation under the statute but had not been returned to the U.S. Treasury. The remaining program, HPRP, had no recaptures as of May 31, 2011.

ARRA included specific expenditure and reallocation requirements, which varied by program. Therefore, each ARRA program had specific expenditure requirements that had to be met to ensure compliance with the statute. HUD recaptured funds from grantees that did not comply with expenditure requirements or failed to meet performance requirements. Therefore, in accordance with Title XIII, Pay It Back Act, of the Dodd-Frank Act, enacted on July 21, 2010, HUD must return ARRA funds recaptured after the enactment date to the general fund of the U.S. Treasury.

In our report, 2011-FO-0005, HUD Can Improve Its Oversight of ARRA Obligation and Expenditure Requirements, issued May 20, 2011, we recommended that HUD return $1.6 million in deobligated ARRA funds to the U.S. Treasury in accordance with the Pay It Back Act. A HUD memorandum, issued to the Office of Inspector General (OIG) on April 25, 2011, entitled "OIG's Draft Audit Report HUD Can Improve Its Oversight of ARRA Obligation and Expenditure Requirements," generally concurred with our recommendation and cited recognition of sound cash management practice for the immediate return of recaptured funds.

We reviewed the expenditure and recapture reports for the six ARRA programs as of May 31, 2011, to determine whether the reports existed and were accurate and complete. We also determined the recapture rate as a percentage of the appropriated amount. We identified recaptured funds that must be returned to the U.S. Treasury as indicated in table II below.

Table II. ARRA recaptures as of May 31, 2011

ARRA program area	Appropriated	Recaptured	Recapture percentage[3]
HPRP	$1,500,000,000	$0	0%
TCAP	2,250,000,000	$0	0%
Public Housing Capital Fund - formula	3,000,000,000	2,021,326	0.1%
Public Housing Capital Fund - competitive	1,000,000,000	14,061,781	1.4%
Lead Hazard Reduction program	100,000,000	4,514,310	4.5%
Native American Housing Block Grant - formula	255,000,000	252,880	0.1%
Total	$8,105,000,000	$20,850,297	0.3%

The $20.85 million in recaptured funds is less than 1 percent of the total amount of ARRA funds available for obligation for the six programs under review.

As the purpose of ARRA funds was to stimulate the economy, the return of recaptured funds in a timely manner would be beneficial to the public. These funds could be made available toward other government programs or deficit reduction. Additionally, the immediate return of the recaptured and deobligated funds would eliminate the need for additional resources to track funds that are no longer eligible for use by HUD. Further, while the recaptured funds had been identified, prudent cash management practices would require the efficient return of recaptured funds. It would also require the identification of funds for need and the recapture of those funds not needed or ineligible for reallocation in a timely manner.

[3] Percentages are rounded

CPD Had No Plans To Award $6.2 Million in Unobligated TCAP Funds

More than $6.2 million in deobligated TCAP funds remained unobligated, and CPD had no plans to obligate the funds before the expenditure deadline. Specifically, $16.4 million in TCAP funds was deobligated in fiscal year 2009, and $10.1 million was reallocated in March 2011; however, the remaining $6.2 million had not been reallocated as of May 31, 2011. The funds were recorded in HUD's accounting records as unreserved and unobligated funds. In discussions with CPD program staff, staff members indicated that reallocations were based on performance and there were no projects in which to reallocate the remaining deobligated funds. Therefore, CPD program staff members stated that they had no plans to reallocate and obligate the funds and expected to let funds remain unobligated until the fund expired.

In accordance with Public Law 111-203, HUD must return recaptured or deobligated ARRA funds that were unobligated as of July 21, 2010 to the General Fund of the U.S. Treasury by December 31, 2012. While the TCAP funds were recaptured before the Pay It Back Act enactment date, the CPD program office acknowledged that the funds would not be reallocated and obligated. Therefore, the $6.2 million in TCAP funds should be returned to the U.S. Treasury to accelerate the use of funds toward other government programs as there is no purpose in retaining the funds on HUD's books. The timely return of the funds will fulfill the spirit for which ARRA was intended which is to benefit the needs of the public.

Conclusion

HUD recaptured $20.85 million in ARRA funds for failure to meet performance and expenditure requirements, which must be returned to the U.S. Treasury in accordance with the Pay It Back Act. Additionally, $6.2 million in deobligated TCAP funds should be recaptured and returned to the U.S. Treasury.

Recommendations

We recommend that the Office of the Chief Financial Officer

2A. Within 60 days of the date this report is issued, return to the U.S. Treasury $20,850,297 in recaptured ARRA funds in accordance with the provisions of the Pay It Back Act.

We recommend that the the Office of Community Planning and Development

2B. Recapture $6,223,557 in TCAP funds and return the funds to the U.S. Treasury.

Finding 3: ARRA Grant Closeout Policies and Procedures Were Inconsistent With ARRA Requirements

The grant closeout process for two of the six programs reviewed was inconsistent with ARRA expenditure requirements. HUD's initial guidance to ARRA program offices for the drawdown of ARRA funds allowed the withholding of funds until after the grant period expired, which was inconsistent with ARRA expenditure requirements. If the policies and procedures are not amended, funds may be withheld beyond the expenditure deadline, resulting in HUD's failure to comply with ARRA expenditure requirements.

Lead Hazard Must Amend Its Grant Closeout Policy

The Lead Hazard Reduction program had grant closeout procedures which allowed for disbursements to be made to grantees after the final expenditure deadline had passed. In accordance with the Policy Guidance 2000-02 and/or GTR instructions for the program and any amendments, HUD reserves the right to withhold five-percent (5%) of the Federal award amount pending the receipt and approval of a Final Report (with supporting documentation) prepared. Specifically, the program's grant closeout policy allowed (1) additional time after the final expenditure deadline for grantees to submit invoices for approval and (2) HUD to withhold five percent of the grant award amount for 90 days after the expenditure deadline. Specifically, the special conditions articles of the Office of Healthy Homes and Lead Hazard Control ARRA grant and cooperative agreement terms and conditions allowed (1) the withholding of five percent of ARRA funds for 90 days after the expenditure deadline and (2) not disbursing the funds to the grantee until the government technical representative reviewed the grantee's final closeout package and approved it. At that time, the remaining five percent of the funds would be disbursed to the grantee.

ARRA, as amended, contains specific expenditure requirements for recipients of ARRA funds. The expenditure requirements for each ARRA program require that a specific percentage of ARRA funds be expended within 2 and 3 years of obligation or the ARRA enactment date. The grants' closeout guidance was based on ARRA expenditure guidance issued by HUD's Office of General Counsel that was revoked. Failure to comply with ARRA requirements could result in funds being recaptured for expenses that had already been incurred, which could negatively impact ongoing projects or activities of the grantee. Based on discussions with program staff, we understand that efforts were being made to amend the policy for distribution to grantees.

TCAP Should Direct Grantees to Follow ARRA Expenditure Requirements for Grant Closeout

The grant closeout policy for some TCAP grantees was inconsistent with ARRA expenditure requirements. In discussions with TCAP program staff, we found that State housing finance agencies' grant agreements with subgrantees allowed the agency to retain a percentage, typically 10 percent, of ARRA funds from subgrantees until the end of the grant closeout period. However, HUD was unable to provide specific details to determine the number of agencies retaining funds and the amount withheld because HUD was unaware that grantees' were implementing this practice. Although the extent of the problem is unknown, this practice increased the risk of housing finance agencies' performing a drawdown of the retained funds after the expenditure deadline, which was not consistent with ARRA expenditure requirements.

ARRA, as amended, requires that all funds be expended within 3 years of obligation. Each ARRA program has specific expenditure deadline dates before which the drawdown of all ARRA funds must be completed. The withholding of funds beyond this date is inconsistent with this requirement. HUD's failure to direct housing finance agencies to amend this policy for ARRA funds placed HUD at risk for noncompliance with ARRA expenditure requirements.

Conclusion

The Office of Healthy Homes and Lead Hazard Control must amend the grant closeout policy for Lead Hazard Reduction ARRA recipients, and the Office of Community Planning and Development must direct TCAP ARRA grantees to ensure that funds are not retained beyond the expenditure deadlines. If the policies and procedures are not amended to exclude the withholding of funds beyond the expenditure deadline, ARRA receipients may not receive funds for eligible costs.

Recommendations

We recommend that the Office of Healty Homes and Lead Hazard Control

3A. Direct the Lead Hazard Reduction program to amend its internal grant closeout policy for consistency with ARRA requirements.

We recommend that the Office of Community Planning and Development

3B. Direct TCAP grantees to amend grant closeout procedures to ensure compliance with ARRA expenditure requirements.

Finding 4: ARRA Funds Control Plans Did Not Include Pay It Back Act Requirements

The funds control plan for HUD ARRA programs had not been appropriately modified to include the requirements set forth in the Pay It Back Act. Two of the six programs reviewed had not modified their funds control plans, and the remaining four programs had not had their modified plans reviewed and approved by OCFO. The reason why two programs did not modify their funds control plans is because one indicated that the Pay It Back Act requirements were not applicable to its program and the second stated that reallocation and recapture requirements were not originally included in the plan, and therefore, did not need to be updated. The remaining four plans had been modified but not approved because one had been submitted to OCFO almost 11 months after the passage of the act. For the remaining three, OCFO had provided the program offices comments and suggested changes and were waiting for the plans to be resubmitted for final review. The failure to update the funds control plans with Pay It Back Act requirements put program offices and HUD at risk for noncompliance with the Act. Further, it hinders HUD's ability to ensure proper control of funds at all levels and affix responsibility for violations of the Anti-Deficiency Act[4].

Final Funds Control Plans Did Not Include Pay It Back Act Requirements

The funds control plan for HUD's ARRA programs had not been appropriately modified to include Pay It Back Act requirements. Specifically, the funds control plans for the HPRP and TCAP program had not been modified to include Pay It Back Act requirements. The plans for the remaining four programs, Public Housing Capital Fund (formula and competitive), Native American Housing Block Grant (formula), and Lead Hazard Reduction had been updated and submitted to OCFO for review and approval. However, the Lead Hazard Reduction funds control plan was not modified until May 10, 2011, almost 10 months after the passage of the Pay It Back Act. Additionally, OCFO had not completed its review and approved the remaining three plans as of June 30, 2011, 11 months after the passage of the Pay It Back Act. OCFO stated that they had submitted comments and suggested changes to the plans. They were waiting for the program offices to finalize and resubmit the plans for final review.

The Federal Managers' Financial Integrity Act of 1982 requires that internal accounting and administrative controls of each executive agency be established to ensure that obligations and costs comply with applicable law. Additionally, the

[4] U.S. Code, Title 31 Section 1518 - adverse personnel actions; Section 1519 - criminal penalty provides adverse personnel actions and criminal penalties for any officer or employee that violates the requirements of expenditures and obligations.

fiscal year 2003 Appropriations Act states, "That the Chief Financial Officer shall establish positive control of and maintain adequate systems of accounting for appropriations and other available funds as required by 31 U.S.C. [United States Code] 1514." Lastly, HUD Handbook 1830.2 requires that the allotment holder "develop, maintain and enforce adequate funds control plans." Further, it affixes responsibility to the CFO to "require and approve up-to-date funds control plans from all allotment holders."

OCFO did not complete its review of the revised funds control plans and concur with the revisions in a timely manner to ensure compliance with Pay It Back Act requirements. Additionally, program offices had not modified the plans to include the significant change in the program, as required, and had improperly certified to OCFO that the previously approved plans were still valid and consistent with applicable laws, policies, procedures, and current funds control processes.

The failure to update the funds control plans with Pay It Back Act recapture requirements put the program offices at risk for noncompliance with the Act. These plans should provide a significant source of guidance on compliance with ARRA expenditure requirements and other applicable laws and regulations. The lack of clear policies or procedures for the return of funds to the U.S. Treasury could result in HUD's becoming noncompliant with these requirements. Also, this practice caused HUD to be inconsistent with best practices for cash management.

Conclusion

Two programs—the HOME Investment Partnerships Program (TCAP), and HPRP—had not modified their funds control plans, and four programs— the Native American Housing Block Grant, Lead Hazard Reduction, and Public Housing Capital Fund (formula and competitive)—had modified the funds control plans to include Pay It Back Act requirements. However, the Lead Hazard Reduction program plan was not modified until almost 10 months after the passage of the act and the other three plans that had been modified had not been reviewed and approved by OCFO. The failure to update the funds control plans with Pay It Back Act requirements put the program offices and HUD at risk for noncompliance with the Act. Further, it hinders the ability of OCFO to properly monitor, account for, and process ARRA funding and recapture requests and affix responsibility for any possible Anti-Deficiency Violations.

Recommendations

In an earlier report, 2011-FO-0003, Additional Details To Supplement Our Report On HUD's Fiscal years 2010 and 2009 Financial Statements, issued on November 15, 2010, we recommended that HUD establish and implement procedures to ensure accuracy and completeness of ARRA funds control plans. We recommend the Office of the Chief Financial Officer,

4A. Complete the review of the funds control plan for ARRA Native American Housing Block Grant formula grants, Lead Hazard Reduction grants, ARRA Public Housing Capital Fund formula grants, and ARRA Public Housing Capital Fund competitive grants and concur or nonconcur with the revisions.

4B. Direct HPRP and the HOME Investment Partnerships Program (also known as TCAP), to revise their funds control plans to ensure compliance with ARRA and Pay It Back Act requirements.

4C. Complete the review of all other ARRA funds control plans to determine whether any remaining program offices have not provided updates to include Pay It Back Act requirements and direct program offices identified in this review to revise their funds control plans to ensure compliance with ARRA and Pay It Back Act requirements.

SCOPE AND METHODOLOGY

ARRA provided for supplemental appropriations for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, and State and local fiscal stabilization for the fiscal year ending September 30, 2009. Each program area had specific expenditure requirements, which we considered in planning the review. This review's intent was to determine compliance with ARRA expenditure requirements as of May 31, 2011. In addition, we reviewed HUD's progress in the expenditure of funds for programs which had not reached their expenditure deadline as of May 31, 2011. Further, we reviewed the timing of funds recaptured and expended to determine compliance with the Pay It Back Act.

The programs in our review included the (1) HOME Investment Partnerships Program (TCAP), (2) Public Housing Capital Fund (formula), (3) Public Housing Capital Fund (competitive), (4) HPRP, (5) Native American Housing Block Grant (formula), and (6) Lead Hazard Reduction program. We selected these programs for review based on the initial expenditure deadline for each program. The initial expenditure deadline varied for each program; therefore, the programs were selected based on which programs would have a substantial amount of its grantees reach its initial expenditure deadline as of May 31, 2011.

We obtained the funds control plans for the programs that received ARRA funding from OCFO to determine whether the plans had been appropriately modified to include Pay It Back Act requirements for rejected, rescinded, and withdrawn funds.

From OCFO, we obtained the appropriated, obligated, unobligated, percentage unobligated, and disbursed amounts for the programs reviewed to determine whether HUD expended ARRA funding in accordance with ARRA requirements. We requested all HUDCAPS[5] expenditure and recapture data for the period March 1, 2009, through May 31, 2011, for all six ARRA appropriations under review.

From each program office under review, we requested a detailed listing of total obligations, total disbursements, and grant obligation dates as of May 31, 2011, for all grantees of ARRA funds. We also requested a detailed listing of ARRA funds that were identified by the program office as recaptured as of May 31, 2011.

We also interviewed HUD's staff from the Office of Strategic Planning and Management, CPD, OCFO, the Office of Affordable Housing and Preservation Programs, and the Office of Public and Indian Housing.

We used the information requested to determine whether (1) ARRA recipients met or were expected to meet their initial expenditure requirements; (2) funds that were rejected, rescinded, or withdrawn had been properly recaptured and were no longer available for obligation; (3) funds control plans had been appropriately updated with Pay It Back Act requirements; and (4) HUD

[5] HUD's Central Accounting Program System

had adequate oversight activities in place to ensure that ARRA recipients met their expenditure requirements.

We assessed the reliability of OCFO's and the program offices' data by performing reconciliations between the two sets of reports and determining the cause for any differences. We determined that the data were sufficiently reliable for the purposes of this audit.

We performed our audit work from April through August 2011 at the HUD offices located at 451 7th Street SW, Washington, DC. The audit covered the period March 31, 2009, through May 31, 2011, but was expanded when necessary to include other periods.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objectives:

- Controls over the recapture process for ARRA grants.
- Documentation of administrative controls implemented to monitor ARRA funds.
- Grant closeout procedures implemented for ARRA grantees.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- Administrative control documentation did not comply with requirements that OCFO require and approve up-to-date funds control plans for ARRA programs (finding 4).

FOLLOW-UP ON PRIOR AUDITS

HUD Can Improve Its Oversight of ARRA Obligation and Expenditure Requirements, 2011-FO-0005

In our report, 2011-FO-0005, HUD Can Improve Its Oversight of ARRA Obligation and Expenditure Requirements, issued May 20, 2011, we reported $1.6 million in recaptured funds that must be returned to the U.S. Treasury. The Pay It Back Act amended the recapture and reallocation provisions previously required in the statute and required the return of recaptured funds. HUD concurred with our recommendation and planned to return the recaptured funds to the U.S. Treasury within 60 days of the issuance of the final report. During our review, we found that HUD was not returning recaptured funds processed post-Pay It Back Act to the U.S. Treasury.

Additional Details To Supplement Our Report on HUD's Fiscal Years 2010 and 2009 Financial Statements, 2010-FO-0003

In our report, 2010-FO-0003, Additional Details To Supplement Our Report on HUD's Fiscal Years 2010 and 2009 Financial Statements, issued November 15, 2010, we reported as a significant deficiency that "HUD needs to improve administrative control of funds." In that report, we found that funds control plans were not updated to reflect changes in accounting procedures, allotment holders, or funds control officers and requirements were not always followed to support the obligation and disbursement of funds. During our review, we found that OCFO did not complete its review of the revised funds control plans and concur with the revisions in a timely manner to ensure compliance with Pay It Back Act requirements.

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Funds to be put to better use 1/
2A	$20.85 M
2B	$6.2 M

1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. The recommendation is necessary to ensure the use of funds toward other activities, which will support the mission of the Act.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-3000

OFFICE OF THE CHIEF FINANCIAL OFFICER

SEP 27 2011

MEMORANDUM FOR: Thomas R. McEnanly, Director, Financial Audits Division, GAF

FROM: David Sidari, Acting Chief Financial Officer, F 9/27/11

SUBJECT: Management Comments on the Draft Audit Report on American Recovery and Reinvestment Act Funds Issued September 15, 2011

Thank you for the opportunity to review and comment on the subject draft audit report. We appreciate the work of the Office of the Inspector General (OIG) and are pleased that this draft audit report did not identify any new significant deficiencies in the Department's management of the funds reviewed and disbursed under the American Recovery and Reinvestment Act (ARRA) of 2009. We are particularly pleased that Finding 1 of the report recognized that five of the six ARRA programs included in the review met their expenditure requirements and the sixth program substantially met its requirement with a 93.2 percent success rate. Consequently, the audit correctly concluded that the six programs were in general compliance with ARRA expenditure requirements.

Comment 1

Regarding recommendations 2A and 2B; we agree with returning the $20.85 million to the Treasury and plan to do this in conjunction with the end of the fiscal year. We also believe the $20.85 million should not be identified in Appendix A as ineligible as the funds were not misspent or misused. In addition, we are working with the Office of Community Planning and Development to return the $6.2 million in Tax Credit Assistance Program funds to Treasury this fiscal year as well.

Comment 2

In response to recommendation 3A, the Office of Healthy Homes and Lead Hazard Control (OHHLHC) will ensure that the Recovery Act closeout requirements are met. OHHLHC plans to amend the grant award agreements for ARRA grantees to ensure compliance with the Recovery Act and HUD regulations. The OGC opinions of January 24, 2011 and July 21, 2011 will be incorporated in the appropriate provisions of the grant award, as well as guidance received on further clarification from OMB and OGC on the reimbursement of expenditures incurred during the period of performance and liquidated within 90 days after the end of the funding period. The OHHLHC believes their Policy Guidance 2000-2 does not require amendment as the award agreement order of precedence (Article 36 of OHHLHC grant award agreement) states that Recovery Act requirements supersede other requirements.

Comment 3

CPD disagrees with OIG recommendation 3B that asks grantees to amend their grant closeout procedures to ensure compliance with ARRA expenditure requirements. As described in the detailed attachment, CPD believes these closeout procedures are not related to project completion including the final expenditure of funds on a project-specific basis.

Comment 4

Finally, we would like to point out that the three recommendations related to the funds control plans are being addressed through existing corrective action plans in response to the audit of

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example, recommendation 2011-FO-0003-5B asks HUD to establish and implement procedures to ensure the accuracy and completeness of ARRA funds control plans, while recommendation 5I asks HUD to perform a review of all funds control plans to ensure they are up to date. The Office of the Chief Financial Officer has corrective action plans in place and continues to actively work with the affected offices to bring their ARRA funds control plans current with the Pay It Back Act. While we acknowledge competing priorities have impacted the pace of implementation of corrective actions, we do suggest that OIG review the existing open funds control recommendations and consider deleting the three identified in Finding 4 of the draft report.

I would like to thank you and your staff and express our appreciation for your efforts to improve HUD's management of ARRA funds. Should you have any questions regarding our response, please contact Frank Murphy on extension 3466 or Jerry Vaiana on extension 8106.

Attachment

Attachment

Comments on Draft Audit Report: ***American Recovery and Reinvestment Act of 2009 Grantees Met Initial Expenditure Requirements, but HUD Should Return Recaptured Funds to the U.S. Treasury and Ensure That Grant Closeout Procedures Comply With the Act.***

Comment 5

Tax Credit Assistance Program (HOME Investment Partnerships Program)

Comment 1 - Page 14, "we recommend that the Office of Community Planning and Development recapture $6,223,357 in TCAP funds and return the funds to the U.S. Treasury." CPD deobligated these funds as referenced on page 13 of the Draft Audit Report. Hence, these funds have already been recaptured. Of the total amount recaptured from TCAP grantees, OAHP reallocated approximately $10 million. At the time of the meetings between OAHP and OIG, OAHP just completed its attempts at reallocating the remaining $6.2 million of recaptured TCAP funds to additional TCAP grantees. Both the recapture of unused TCAP funds and CPD's decision to reallocate recaptured TCAP funds were made prior to enactment of the Pay It Back Act. In fact, according to the statute, TCAP funds "remain available until September 30, 2011". OAHP does not recall stating the office expected to let funds remain unobligated until the funds expired. However, as mentioned above, OAHP recaptured these funds, reallocated the funds it could, and the unobligated balance is in the TCAP account available to be returned to the U.S. Treasury by the CFO. These funds are no longer obligated or reserved to TCAP grantees. A better characterization of the comment would be that OAHP does not have the ability to send the unused TCAP funds to the U.S. Treasury and that CFO would return the funds to Treasury either after September 30, 2011 or February 16, 2012, whichever was appropriate.

Comment 6

Comment 2 - Page 16, first paragraph. OAHP responded to these statements in emails prior to this draft audit report. OAHP is still working on grant closeout policies and has not released any guidance to grantees on this process. In its discussions with OIG, OAHP staff made clear that the practice of retaining a percentage of TCAP funds until the end of the TCAP project (also commonly referred to in housing development as a "retainage") by TCAP grantees is a project specific practice and not a grant specific practice. Consequently, this practice is in no way related to grant closeout. TCAP grantees enter into a project-specific written agreement with the project owners, not a grant agreement. In contrast, the grant closeout process is between HUD and the TCAP grantees. Project owners are not involved in this process. OAHP has consistently stated and advised grantees that all funds must be expended prior to February 16, 2012. It is clearly stated in the TCAP Notice, TCAP grant agreement, and the ARRA statute, which were provided to IG by OAHP staff. In addition, the TCAP Notice and statute require TCAP grantees to give priority to projects that will be completed by February 16, 2012, ensuring funds will be fully expended by the expenditure deadline. OAHP disagrees with OIG recommendation that grantees amend their grant closeout procedures to ensure compliance with ARRA expenditure requirements. As stated above, these closeout procedures are not at all related to project completion including the final expenditure of funds on a project-specific basis. These grantees have been managing their Low Income Housing Tax Credit (LIHTC) programs for 20 plus years and have followed Section 42 of the Internal Revenue Code as well. The LIHTC program is a Treasury / IRS program that has successfully completed hundreds of thousands of affordable units. This practice of retaining a percentage of funds until project completion is an additional layer of oversight and due diligence in ensuring ARRA funds are spent on projects that are successful and in compliance with the ARRA statute. Currently over 92 percent of TCAP funds have been expended and grantees are on track to expend 100 percent of funds available well before the February 16, 2012 deadline.

OIG Evaluation of Auditee Comments

Comment 1 HUD generally concurred with our recommendation to return $20.85 million in recaptured ARRA funds to the U.S. Treasury. Additionally, HUD has generally concurred with our recommendation to recapture and return $6.2 million in Tax Credit Assistance Program funds to the U.S. Treasury. However, HUD did not agree with the classification of the recaptured funds as ineligible costs. OIG reviewed the classification of the costs and determined that the recaptured funds are more appropriately classified as funds put to better use.

Comment 2 HUD generally agrees with the finding but does not concur with our recommendation to amend the grant closeout policy and procedures for the Lead Hazard Reduction program. OIG believes that the incorporation of the OGC opinion issued July 21, 2011, if appropriately included, will amend the closeout policy and procedures as recommended. However, the inclusion of OGC opinion issued January 24, 2011 should only be incorporated to the extent referenced in the OGC opinion July 21, 2011. Specifically, the July 2011 opinion refers the reader to the definition of expenditures as documented in the opinion issued January 24, 2011. Any further references to the January 2011 opinion will not reasonably address OIG's recommendation. Additionally, OIG concurs with OHHLHC that any updated guidance received from OMB and OGC regarding the expensing of Recovery Act funds for administrative fees should be included in the policy guidance.

Comment 3 HUD does not concur with our recommendation to amend the grant closeout policy and procedures for the Tax Assistance Credit Program. OIG disagrees with CPD's assertion that the current grant closeout procedures will not effect the final expedentiture of funds. The timing of the performance of closeout procedures, which include the final drawdown of retained funds, present a possible risk that obligated funds will be recaptured and swept by the U.S. Treasury before the retained funds are drawn down for payment to the grantee. The recapture of the funds for expenses already incurred poses a risk that HUD will have to use non-ARRA resources to fulfill its obligation to the grantees. Further, TCAP program staff have indicated that they are unaware of the number of State Finance Agencies that are retaining funds and the amount of funds that are retained. Therefore, OIG does not believe that sufficient information is available to assert that the risk is reasonably mitigated as CPD indicates in the Attachment.

Comment 4 HUD concurs with the finding; however, HUD requests that OIG remove the related recommendations because a similar finding was reported in the OIG audit report 2011-FO-003 issued November 15, 2010. OIG will not remove the recommendations, however OIG will close out the recommendations once the final actions have been completed from the prior year report.

Comment 5 In a meeting with TCAP program staff on June 14, 2011, OIG was informed that the $6.2 million would be returned to the Treasury at the end of the program. Further, on August 1, 2011, OIG received an email communication from TCAP program staff that stated that the $6.2 million is reported as unreserved/unobligated on the status of funds report because CPD still has the option to award them to other grantees. Therefore, CPD intended that the funds remain on HUD's books until the obligation requirement expired, which is September 30, 2011. Additionally, CPD did not recapture[6] the funds or indicated to HUD's Accounting Division that the funds should be recaptured and returned to the U.S. Treasury because the current status of the funds does not allow HUD to return the funds to the U.S. Treasury. OIG acknowledges that CPD deobligated the $6,223,557 of ARRA funds as reported in this report. However, OIG disagrees with the characterization that the funds have already been recaptured.

OIG understands from the CFO comments to this report that it is working with the CPD program staff to recapture the funds. The CFO comments would suggest that the CFO is aware that the funds are not appropriately classified as recaptured for the purposes of the returning the funds to the U.S. Treasury. In this report, OIG is recommending that CPD recapture the funds in the manner required to inform HUD's Accounting Division that the funds have been recaptured for the purposes of returning the funds to the U. S. Treasury.

Comment 6 OIG disagrees with CPD that the retention of funds is not related to the grants closeout process. During the grant closeout process, costs may be found to be ineligible due to the expensing of funds after the expenditure deadline. While the likelihood of this issue is unknown, the risk of the occurrence is the basis of OIG's recommendation. Additionally, in email communications OIG received from TCAP program staff, they indicated unawareness of the number of grantees that were retaining a percentage of funds and expressed the difficulty in determining which grantees retain funds. Further, as documented in the TCAP grant agreement, "The Grantee is responsible for the use of its TCAP grant. The use of subgrantees or contractors does not relieve the Grantee of this responsibility. Grantees are responsible for managing the day-to-day operations of grant and subgrant activities."

The TCAP grant program was established in 2009 as a new program with new requirements which must be met to ensure compliance with ARRA. CPD acknowledges in the Attachment that it has not released any grant closeout guidance to the grantees. Therefore, guidance must be provided to the grantees to ensure that the information is communicated to the project owners to ensure compliance with ARRA.

[6] For accounting purposes, deobligated funds are not processed in the same manner as recaptured funds. Specifically, the transaction code entered to recapture the funds that are not eligible for reallocation or will not be reallocated is different than the transaction code used for the deobligation of funds. Therefore, HUD's Accounting Division would require the $6.2 million be processed as a recapture that will not be reallocated so that the funds may be returned to the U.S. Treasury.