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TO: Pat McCauley, Director, Community Planning and Development Division,  
Omaha Program Center, 7DD

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FROM: Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

SUBJECT: The State of Nebraska Did Not Close HOME Projects in a Timely Manner

## **HIGHLIGHTS**

### **What We Audited and Why**

We reviewed the HOME Investment Partnerships Program (HOME), administered by the State of Nebraska's Department of Economic Development (State), in Lincoln, Nebraska. We audited the State because a recent U.S. Department of Housing and Urban Development (HUD) HOME risk assessment ranked the State as a high-risk recipient in HUD's Region VII.

Our objective was to determine whether the State was closing HOME-funded projects in accordance with HUD requirements.

### **What We Found**

The State did not close HOME projects in HUD's computer systems in a timely manner. It has made progress in properly closing several hundred past due projects, but many past due projects remain unresolved.

### **What We Recommend**

We recommend that HUD verify that the State implements appropriate controls to ensure that it closes HOME projects in HUD's data systems within the required

timeframes. We also recommend that HUD monitor the State's progress in closing projects currently exceeding HUD's required timeframes and ensure that the projects are closed properly and expeditiously.

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**

The State agreed with our conclusions. We provided the report to the State on February 26, 2007, and requested a response by March 9, 2007. The State provided written comments on March 13, 2007.

The complete text of the auditee's response can be found in appendix A of this report.

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## BACKGROUND AND OBJECTIVES

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The U.S. Department of Housing and Urban Development (HUD) HOME Investment Partnerships Program (HOME) is the largest federal block grant to state and local governments designed exclusively to create affordable housing for low-income households. Each year it allocates approximately \$2 billion among the states and hundreds of localities nationwide. Among the recipients of HOME funds is the State of Nebraska. Nebraska's Department of Economic Development (the State), located in Lincoln, Nebraska, administers the HOME program for the state. The State does not directly administer the program but grants the funding to subrecipients to accomplish program objectives. Subrecipients are public agencies or nonprofit entities selected by recipients to administer HOME funds.

The State receives HOME funding annually from HUD and invests the funds in the following housing activities:

- Homeowner rehabilitation: Assists owner-occupants with the repair, rehabilitation, or reconstruction of their homes.
- Homebuyer activities: Finance the acquisition and/or rehabilitation or new construction of homes for homebuyers.
- Rental housing: Acquires and/or rehabilitates or constructs affordable rental housing.

For the State's fiscal years 2004 through 2006, HUD provided it more than \$16.5 million in HOME funding.

<b>Fiscal year</b>	<b>HOME Investment Partnerships Program</b>	<b>HOME American Dream Downpayment Initiative</b>	<b>Total</b>
2004	\$ 5,485,713	\$517,055	\$ 6,002,768
2005	\$ 5,333,377	\$159,591	\$ 5,492,968
2006	\$ 5,010,987	\$ 79,635	\$ 5,090,622

Our objective was to determine whether the State was closing HOME-funded projects in accordance with HUD requirements, including closing individual projects in HUD's HOME fund tracking system, the Integrated Disbursement and Information System.

## RESULTS OF AUDIT

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### Finding: The State Did Not Close HOME Projects in a Timely Manner

The State did not close HOME projects in HUD's computer systems in a timely manner. This deficiency occurred because the State did not have adequate controls in place to ensure that it followed applicable laws and regulations. Failure to properly update HUD's data caused HUD to understate HOME accomplishments nationally, negatively affected the State's performance ratings, and can cause unnecessary hardships on project owners receiving HOME funds to provide affordable housing for low-income families.

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#### **Projects Were Not Closed within the Required Timeframe**

The State did not close HOME projects in HUD's computer systems within the HUD-required timeframe. Regulations at 24 CFR [*Code of Federal Regulations*] Part 92 provide that a HOME-funded project is not complete until it complies with all HOME requirements and the recipient has entered the required information into HUD's Integrated Disbursement Information System. Recipients must enter the required information into HUD's data systems within 120 days after the final drawdown of HOME funding, or the project is considered past due.

In 2004, HUD notified the State that it was not properly closing projects in HUD's data systems. At that time, HUD identified several hundred projects for which all awarded funds had been drawn down for more than 120 days but the State had not closed the projects in HUD's systems.

The State began taking steps to rectify the deficiencies, and by September 30, 2006, only 51 past due projects remained unresolved. However, the past due projects had increased to 66, involving HOME funds of more than \$2.9 million, as of November 30, 2006. A comparison of the two monthly reports showed that the State had successfully closed 10 past due projects in October and November, but another 25 projects had become past due by the time the November report was issued. This information indicates that the State is not making consistent progress in resolving past due projects in HUD's systems or ensuring that it is currently closing projects within the 120-day deadline.

### **Controls Were Not Adequate to Ensure Proper Closure of HOME Projects**

The State lacked adequate controls to ensure that it closed projects in HUD's data systems within the required 120-day timeframe. This problem occurred because the State's staff was not aware of all data entry steps needed for their internal system to accurately update and close projects in HUD's systems. Therefore, they did not recognize that they had not fully closed the projects in HUD's data systems until HUD notified the State in 2004 of its numerous past due projects.

In addition, the State's policies and procedures allowed subrecipients to draw down all HOME funds granted for rental housing projects without ensuring that the rental units were occupied. When a recipient closes a rental project that has vacant units in HUD's systems, it negatively affects the recipient's HOME performance ratings. The State was not closing completed rental projects until the project was fully occupied, which sometimes caused it to exceed the 120-day timeframe. According to the State, it has recently corrected this problem by changing its policies and procedures to require that it retain 10 percent of a rental housing project's funding until the units have tenants. Once the units are occupied, the State will release the retained funding as the final drawdown and close the project in HUD's systems.

The State's policies and procedures also did not ensure that it obtained the activity completion reports from subrecipients. Its policy was to disallow additional funding to subrecipients until they provided the reports. However, some subrecipients still did not comply. Without the reports, the State did not have the data needed to close projects in HUD's systems. According to the State, it has improved its process for obtaining the reports.

Further, the State could not close approximately five of the oldest past due projects due to computer programming errors. According to the State, it is working with HUD to resolve the issue.

### **HUD and the State Understated HOME Accomplishments and Caused Unnecessary Hardships**

By not implementing adequate controls that ensure complete and timely closure of HOME projects, the State is understating its true accomplishments and negatively affecting its HOME performance indicators and rankings. It is also causing HUD to understate HOME accomplishments nationally.

Further, these problems can cause project owners receiving HOME funds to have to provide affordable housing longer than necessary. Regulations at 24 CFR [Code of Federal Regulations] Part 92 explain that a project's affordability period does not begin until the project is completed, the final drawdown of HOME funds awarded has been made, and all required data have been recorded in HUD's systems. The affordability period is the length of time that a project owner receiving HOME funds must abide by HUD's homeowner income limits on properties acquired or rehabilitated with HOME funds (excluding owner-occupied projects) or abide by HUD's rental limits on rental properties.

Because the affordability period begins when the project is fully closed in HUD's data systems, any delays cause the project owner to have to extend the period that the owner is committed to providing affordable housing to eligible persons. Therefore, project owners cannot provide the housing to persons with income that exceeds HUD's income limits, nor can the owners raise the tenant rents beyond HUD's limits. This places an unnecessary burden on the project owner.

## Conclusion

The State has made progress in resolving past due projects. However, it still needs to resolve remaining past due projects and improve its controls to ensure that completed projects are consistently closed in HUD's data systems within the 120-day required timeframe.

## Recommendations

We recommend that the director, Community Planning and Development Division, Omaha Program Center,

- 1A. Verify that the State implements appropriate controls to ensure that it closes HOME projects in HUD's data systems within the required 120-day timeframe.
- 1B. Monitor the State's progress in closing projects currently exceeding the 120-day timeframe and ensure that the projects are closed properly and expeditiously.

## SCOPE AND METHODOLOGY

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Our review generally covered the period from July 1, 2003, through June 30, 2006. We began our review by obtaining information on the State's policies and processes for awarding, monitoring, and closing subrecipient grants. Early in the review, we identified concerns with the State's efforts in closing projects; therefore, we focused our efforts in that area.

To achieve our objective, we conducted interviews with the State's staff and staff of HUD's Omaha Office of Community Planning and Development. We reviewed the State's policies and procedures, hard-copy and computer-generated subrecipient grant files, and annual and consolidated plans. We reviewed federal regulations, HOME performance reports and program notices on HUD's Web site, and previous HUD reviews of the State's operations. We also compared the State's hard-copy and computer-generated grant records to HUD's Integrated Disbursement Information System data.

We evaluated the State's actions in closing projects for 10 HOME grants. For its fiscal years 2004 and 2005, the State awarded 49 grants to subrecipients, totaling more than \$8.7 million. Nine of the subrecipients had spent all of their awarded funding, more than \$2.2 million. We reviewed the five highest dollar grants (totaling \$2 million) to evaluate the State's process for closing projects. Based on the results of our initial review, we reviewed an additional five grants. The State closed 205 grants in its fiscal years 2005 and 2006. We reviewed the five most recently awarded grants (totaling \$1.7 million). Nebraska awarded these grants in its fiscal year 2003.

We relied on computerized data contained in HUD's Integrated Disbursement Information System. We assessed the reliability of the data, performed sufficient tests of the data, and found the data adequate to meet our audit objective. We also relied on the State's computerized data to identify subrecipient grants for review. We conducted sufficient tests of the data and found the data adequate to use in selecting grants for review.

We performed on-site work at Nebraska's Department of Economic Development in Lincoln, Nebraska, from July through November 2006. We performed our review in accordance with generally accepted government auditing standards.

# INTERNAL CONTROLS

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Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

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## Relevant Internal Controls

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

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure compliance with HUD's regulations regarding closing HOME projects.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

## Significant Weaknesses

We did not identify any significant weaknesses.

## Appendix A

### AUDITEE COMMENTS

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**The Housing Manager of the State Community and Rural Development Division provided the following comments on March 13, 2007, via e-mail:**

Thank you for the opportunity to provide comments regarding the HUD-OIG Draft report.

As is referenced in the report, the State of Nebraska Department of Economic Development has been improving internal processes in order to achieve full compliance with the requirement to complete projects within 120 days of the final drawdown of funds on each project. The department, in cooperation with the HUD Omaha field office, will evaluate and amend policies as needed to obtain the necessary information from the department's grantees that will ensure that all data entered in the Integrated Disbursement and Information System is both timely and accurate.