



Issue Date	April 13, 2010
Audit Report Number	2010-FW-0002

TO: Dominique Blom, Deputy Assistant Secretary for Public Housing Investments, PI

FROM: *//signed//*
Gerald R. Kirkland
Regional Inspector General for Audit, Fort Worth Region, 6AGA

SUBJECT: HUD's Recapture and Reallocation Plan for Recovery Act Public Housing Capital Fund Grants Had Weaknesses

HIGHLIGHTS

What We Audited and Why

We audited the U. S. Department of Housing and Urban Development's (HUD) compliance with obligation, recapture, and reallocation requirements for the American Recovery and Reinvestment Act of 2009 (Recovery Act) Public Housing Capital Fund program. The audit was in accordance with a mandate to review HUD's awarding, disbursing, and monitoring of Recovery Act funds to determine whether safeguards exist to ensure that grantees use funds for their intended purposes. Our office identified the program as high risk. The audit objective was to determine whether HUD had plans to recapture unobligated Recovery Act Public Housing Capital Fund formula grants¹ (formula grants) and to reallocate the recaptured funds. The audit focused on assessing the adequacy of HUD's specific strategies and whether its plans were consistent with criteria established by the Recovery Act.

¹ These funds have a mandatory obligation deadline of 1 year after award (March 17, 2010, for formula awards).

What We Found

HUD's plan was a generalized description of the process it would undertake to recapture and reallocate formula grant funds not obligated by the March 17, 2010 deadline. It did not contain detailed procedures or timeframes for executing the steps necessary to complete the process. HUD planned to redistribute recaptured formula grant funds to unfunded Recovery Act competitive grant applications. Further, expenditure deadlines may conflict with Recovery Act funding availability.

What We Recommend

We recommend that HUD revise its recapture and reallocation plan to include more detailed procedures for accomplishing HUD's goals and a timeline for completing them and communicate its plan to affected entities. HUD needs to consult with the Office of General Counsel to obtain clarification regarding the conflicting deadlines and to ensure that its plan meets Recovery 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 a copy of the draft report to HUD on March 23, 2010, and requested written comments by March 30, 2010. We held an exit conference with HUD on March 26, 2010. At HUD's request, we extended the date for written comments to April 7, 2010. HUD provided written comments on April 7, 2010. HUD did not agree with parts of the finding but agreed to incorporate our recommendations in future revisions of its plan.

The complete text of HUD's response, along with our evaluation of that response, can be found in appendix A of this report.

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BACKGROUND AND OBJECTIVE

On February 17, 2009, the President signed the American Recovery and Reinvestment Act of 2009 (Recovery Act) into law.² The Recovery Act made supplemental funds available for job preservation and creation, infrastructure investment, energy efficiency and science, assistance to the unemployed, State and local fiscal stabilization for the fiscal year ending September 30, 2009, and other purposes.

The Recovery Act provided \$4 billion³ for public housing agencies to carry out capital and management activities,⁴ including modernization and development of public housing. It allocated \$3 billion for formula grants and \$1 billion for competitive grants. For both grant types, the Recovery Act required public housing agencies to obligate 100 percent of the funds within 1 year of the date on which funds became available to the agency for obligation and expend 60 percent within 2 years and 100 percent within 3 years of such date. Public housing agencies reported their obligations and expenditures using the U. S. Department of Housing and Urban Development's (HUD) Line of Credit Control System (LOCCS).

HUD made Recovery Act formula grants available to public housing agencies on March 18, 2009, resulting in an obligation deadline of March 17, 2010. If a public housing agency failed to comply with the obligation deadline, the Recovery Act required HUD to recapture all remaining unobligated funds awarded to the public housing agency and reallocate such funds to agencies that complied with those requirements. Similarly, HUD was required to recapture and reallocate remaining funds from public housing agencies that failed meet the expenditure deadlines.

HUD awarded \$2.985 billion in formula grants to 3,134 public housing agencies and \$995 million for 396 competitive grants to 211 public housing agencies. HUD received administrative funds under the Recovery Act provisions.

The audit objective was to determine whether HUD had plans to recapture unobligated formula grants and to reallocate the recaptured funds. The audit focused on assessing the adequacy of HUD's specific strategies and whether its plans were consistent with criteria established by the Recovery Act.

² Public Law 111-5.

³ Remaining available until September 30, 2011.

⁴ As authorized under Section 9 of the United States Housing Act of 1937.

RESULTS OF AUDIT

Finding: HUD's Recapture and Reallocation Plan for Recovery Act Public Housing Capital Fund Grants Had Weaknesses

HUD's plan was a generalized description of the process it would undertake to recapture and reallocate formula grant funds not obligated by the March 17, 2010, deadline. HUD should improve its plan by revising it to include more detailed procedures for accomplishing HUD's goals and a timeline for completing them. It should also communicate its plan to ensure that affected entities are aware of its intentions and policies. Further, HUD should build on its experience with the formula grants to establish a standard plan for future recapture and reallocation events. By doing so, it could avoid errors, resolve questions, and be in a better position to defend its actions as being impartial and transparent.

HUD Created a Generalized Recapture and Reallocation Plan

HUD provided a generalized plan to recapture and redistribute unobligated formula grant funds following the March 17, 2010, obligation deadline. HUD's plan would allow public housing agencies 5 working days after the deadline to record eligible obligations into LOCCS, after which time HUD would process an electronic recapture of unobligated funds. HUD planned to redistribute the recaptured formula funds by awarding additional grants to public housing agencies whose applications it did not fund under the competitive grant category for the creation of energy-efficient, green communities (moderate rehabilitation).⁵ HUD did not anticipate recapturing a significant amount of formula funds and held that there would be insufficient funds available to reallocate by formula.

As of January 30, 2010, public housing agencies had not obligated more than \$900 million in formula grants. Because of HUD's considerable effort to ensure that public housing agencies obligated the formula grant funds, between January 30 and March 17, 2010, the agencies obligated all of the remaining funds except for \$3.2 million that 21 agencies returned for various reasons.

It was evident in discussions with HUD staff that they had given thought to many aspects of the reallocation and recapture processes, including consulting with a variety of staff in the Office of Public and Indian Housing (PIH) and the Office of

⁵ HUD funded competitive grants under four categories in a notice of funding availability (NOFA). For the first three categories, it funded applications on a first-come first-funded basis. It rated and ranked applications for two options in category 4, creation of energy-efficient, green communities. Option 1 was for substantial rehabilitation, and option 2 was for moderate rehabilitation. There remained 230 public housing agencies with unfunded applications for category 4/option 2 that met or exceeded the minimum score (60 of 110 points) to qualify for funding under the NOFA.

General Counsel. However, HUD should revise its generalized plan to incorporate more detailed procedures for accomplishing its goals and a timeline for completing them.

HUD Should Establish Detailed Recapture Procedures

To avoid errors and complaints and increase transparency, HUD should define the procedures necessary to recapture funds in accordance with requirements and in a timely manner. For example, it should include a deadline for public housing agencies to appeal to have recaptured funds restored and create target dates for HUD to determine the final amount available for reallocation, select new grantees, and execute grant agreements. The plan should be clear, specific, and unambiguous and should address nuances specific to the Recovery Act grants. It should also plan target dates associated with future recapture and reallocation events resulting from expenditure and competitive grant deadlines.

HUD's plan allowed it to restore recaptured formula funds if a public housing agency provided documentation showing that it did obligate the funds before the deadline. The plan did not disclose how HUD would communicate this with public housing agencies or the circumstances or documentation that it would consider. Further, the plan did not disclose how many days a public housing agency would have to recover the funds. While it might be reasonable to review appeals on a case-by-case basis, HUD should establish and communicate the baseline and documentation for making these determinations. Although this was not a concern for the formula grants, HUD should consider the matter for future deadlines and revise its procedures accordingly.

In another example of areas in which the plan appeared to lack specificity, HUD limited public housing agency administration costs to 10 percent of the grant. This limit should continue to apply to the revised grant total following any recapture of funds. HUD staff commented that they did not want to penalize public housing agencies if they incurred legitimate administrative expenses, such as procurement activities that did not result in contract awards. However, it would be unreasonable to allow public housing agencies that failed to meet obligation requirements to earn more than 10 percent for administration of the grant. HUD should enforce the limit relevant to the revised grant amounts and recapture overages accordingly. It should establish procedures to guide staff in determining the amount subject to recapture.

HUD should also improve the plan related to its electronic recapture process. The plan did not describe the procedures for determining recapture amounts or refer to existing procedures. HUD staff stated that they would electronically deobligate grant funds in HUD's Project Accounting System (PAS), which in turn would reduce grant amounts in LOCCS. HUD field office personnel would then be responsible for making corrections to the individual budget line items for each grant in LOCCS. To ensure a smooth recapture process, HUD should formally

establish or refer to existing procedures to determine amounts subject to recapture, make the recapture, and delineate related staff responsibilities.

Lastly, the plan was silent on the recapture of funds after March 17, 2010, related to public housing agencies' terminating an activity or completing an activity for less than the obligated amount. The plan should address how HUD would recapture and reallocate these funds. The plan mentioned the recapture of funds "mistakenly reported as fully obligated" but did not define this phrase. The plan should define this phrase and describe how it would identify, recapture, and reallocate these funds. As with other recaptured funds, the plan should have clear deadlines and delineate the ability to appeal.

HUD Planned to Reallocate Formula Funds to Competitive Grants

HUD planned to redistribute recaptured formula grant funds to unfunded competitive grant applications.⁶ The plan described the procedures HUD would take to ensure that public housing agencies could still implement the projects in their competitive applications if awarded recaptured funds, including a firm commitment to leverage funds and whether the project remained unfunded. The plan should reiterate that reallocated funds would only go to public housing agencies that were in compliance with the 1-year obligation requirement and HUD's intent to restrict reallocated funds to only one competitive grant per project.⁷ The plan should also include the procedures HUD would use to review grant applications to ensure that it only awards Recovery Act funds for viable, prudent projects to avoid wasteful spending.

HUD Should Plan for Future Recapture and Reallocation Events

The Recovery Act required HUD to recapture and reallocate funds if public housing agencies failed to meet the obligation and expenditure deadlines. HUD should build on its experience with the formula grants to establish a standard recapture and reallocation plan.

For example, the 1-year obligation deadlines for the competitive grants will occur in September 2010, and expenditure deadlines for both grant categories will follow through September 2012 (refer to table below). However, the Recovery Act funds are only available through September 30, 2011. HUD needs to consult with the Office of General Counsel to obtain clarification regarding the conflicting deadlines and to ensure that its plan meets Recovery Act requirements.

⁶ HUD had more than \$240 million in unfunded applications meeting the NOFA requirements.

⁷ The NOFA for the competitive grants restricted awards to one grant per project.

Obligation and expenditure deadlines by grant type

Grant type	Obligation start	Obligation deadline	60% expenditure deadline	Funds available until	100% expenditure deadline
Formula	March 2009	March 2010	March 2011	September 2011	March 2012
Competitive	September 2009	September 2010	September 2011	September 2011	September 2012

By having a standard plan addressing the recapture and reallocation of funds, HUD could easily resolve questions and logistics. HUD would also be in a better position to defend its actions as being impartial and transparent.

Conclusion

HUD's plan was a generalized description of the process it would undertake to recapture and reallocate formula grant funds not obligated by the March 17, 2010, deadline. Under the plan, HUD would redistribute recaptured formula grant funds to unfunded Recovery Act competitive grant applications. However, HUD's plan did not contain detailed procedures or timelines for completing the necessary steps or address future recapture and reallocation requirements. HUD should expand on its plan to recapture and reallocate unobligated formula grant funds by including more detailed procedures and timelines for completing tasks. It should amend its procedures for reallocated funds and use its experience to build on its plans for future recapture and reallocation events.

Recommendations

We recommend that the Deputy Assistant Secretary for Public Housing Investments

- 1A. Revise the recapture and reallocation plan to include more detailed procedures for accomplishing HUD's goals and a timeline for completing them and communicate its plan to ensure that affected entities are aware of its intentions and policies.
- 1B. Consult with the Office of General Counsel to obtain clarification regarding the conflicting deadlines and to ensure that its plan meets Recovery Act requirements.

SCOPE AND METHODOLOGY

We conducted the audit at our offices in Fort Worth, Texas, from January to March 2010. We reviewed the period from March 18, 2009, through March 17, 2010. To meet our objective, we obtained and reviewed relevant laws and implementing guidance, program regulations, HUD policies and procedures, and information HUD posted on its Internet site. We held an entrance conference and requested that HUD provide its written plan to address the obligation deadline and recapture and reallocation procedures. We reviewed HUD's plan to determine its compliance with the Recovery Act and other requirements and the reasonableness and adequacy of the plan. In addition to evaluating HUD's plan, we also took into consideration activities that would take place following the March 17, 2010 formula grant obligation deadline. We interviewed key PIH personnel in the Office of Capital Improvements, the Office of Field Operations, and the Fort Worth, Texas regional office.

We periodically reviewed obligation data from LOCCS and PAS to determine public housing agencies' progress in obligating the formula grant funds. We used the data for background purposes and to gauge public housing agencies' progress in obligating funds as the deadline approached. We did not validate data related to grant obligations because public housing agencies self-reported the information and it was beyond the scope of the audit. We did reconcile the grant amounts in LOCCS and PAS and found them to be in agreement. The data were sufficiently reliable to identify grant amounts and estimate obligation amounts entered by public housing agencies.

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. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objective.

INTERNAL CONTROLS

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

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. They 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:

- Policies and procedures to recapture and reallocate Recovery Act funds in accordance with requirements.

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

Based on our review, we believe that the following item is a significant weakness:

- HUD's recapture and reallocation plan contained insufficient procedures to ensure that it met Recovery Act and other requirements (finding).

APPENDIX

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-5000

HUD LOGO
OFFICE OF PUBLIC AND INDIAN HOUSING

April 7, 2010

MEMORANDUM FOR: Gerald R. Kirkland Regional Inspector General for Audit, Fort Worth, 6AGA

FROM: *//signed//*
Dominique Blom, Deputy Assistant Secretary for Public Housing Investments, PI

SUBJECT: Comments on OIG Draft Audit: HUD Should Improve Its Recapture and Reallocation Plan for Recovery Act Public Housing Capital Fund Grants

Thank you for providing your draft report entitled, "HUD Should Improve Its Recapture and Reallocation Plan for Recovery Act Public Housing Capital Fund Grants," dated March 23, 2010 and for soliciting our input. We have reviewed the draft and offer the following comments for your consideration.

COMMENT 1

Your report focused on how HUD was going to recapture and reallocate the Capital Fund Recovery grants. We recently provided you a detailed recapture plan and, during the audit, we provided you with a description of the reallocation process. Providing a specific time line for the reallocation process during the audit was not possible because the magnitude of the recaptured funds was not known.

There are several sections of the report that do not accurately capture the recapture and reallocation process as provided to you in the Recapture and Redistribution Summary document and the detailed recapture plan recently provided. Please consider revising the following sections:

- Page 6: In the report, the following paragraph references a formal appeal process:

"To avoid errors and complaints and increase transparency, HUD should define the procedures necessary to recapture funds in accordance with requirements and in a timely manner. For example, it should include a deadline for public housing agencies to appeal to have recaptured funds restored and create target dates for HUD to determine the final amount available for reallocation, select new grantees, and execute grant agreements."

COMMENT 2

HUD had prepared an appeal process for housing authorities that challenged the recaptures. This process required the appealing PHA to submit the obligation documents obligating the Recovery Act funds to HUD. After HUD reviewed the documents and concurred that the obligations were correct and obligated by the obligation deadline the PHA would be notified and the funds would be restored to the PHA. If HUD did not concur with the obligations the PHA claimed the PHA would be notified that HUD had denied its appeal and the recapture would stand. However, since no recaptures were electronically processed HUD did not need to implement this process. HUD will add a description in the plan describing the appeal process in subsequent revisions.

- Page 6 and 7: In the following paragraph, the IG indicates that the method to determine the recapture was not clear:

"HUD should also improve the plan related to its electronic recapture process. The plan did not describe the procedures for determining recapture amounts or refer to existing procedures. HUD staff stated they would electronically deobligate grant funds in HUD's Project Accounting System (PAS) which in turn would reduce grant amounts in LOCCS."

COMMENT 3 The plan did not describe the procedures for determining the recapture amounts because LOCCS is the only source for the reported obligations. HUD planned to use the obligation data from the CFO LOCCS information in datamart on March 25, 2010 to determine the recapture amounts. This eliminates any accuracy problems by drawing the data directly from the CFO data. However, given your comment, we will add a description in the plan for clarity for outside reviewers in subsequent revisions.

- Page 10: The below section from the IG report:

"Based on our review, we believe that the following item is a significant weakness: HUD's recapture and reallocation plan contained insufficient procedures to ensure it met Recovery Act and other requirements (finding 1)."

COMMENT 4 We request that the OIG change this assessment from a "significant weakness" to "an area for improvement". We do not agree that there were significant weaknesses or a possibility that HUD would not meet the requirements of the Recovery Act. HUD took measures in LOCCS to prevent any disbursements of unobligated funds after the March 17, 2010 deadline. This was accomplished by preventing PHAs from disbursing from LOCCS amounts above the reported obligation. This provides the first level of protection. The second level of protection was provided by preventing PHAs from reporting obligations for the March 17, 2010 reporting period after 8PM March 24, 2010. This measure, when coupled with the first measure, prevented PHAs from disbursing any funds above the amount obligated by March 17, 2010. This allowed HUD time to process the recaptures without a concern that PHAs would be changing data in LOCCS regarding their obligations. As to the reallocation of funds, the Recovery Act does not specify a specific timeframe by which this must be completed so HUD is compliant with the reallocation requirements of the Recovery Act.

Thank you for providing HUD the opportunity to provide these comments on the draft report. We ask that you please consider incorporating them into the report. Should you have any questions or comments please contact Jeff Riddel at 202-402-7378 or Rick Smith at extension 7652.

OIG Evaluation of Auditee Comments

- Comment 1** We acknowledge that planning for recapture and reallocation was a dynamic process. However, HUD will encounter similar recapture and reallocation requirements in the future with competitive and expenditure deadlines approaching. For effective and efficient program management, HUD should plan for meeting its goals and requirements.
- While the revised recapture plan referred to in HUD's comments appears to be an improvement, HUD should further revise its plan, incorporating items in this report.
- Comment 2** We considered HUD's comments but did not revise the report because the appeal process described was not included in its plan. Further, HUD did not have to electronically process recaptures because the limited number of grantees not in compliance returned formula funds instead of having them recaptured. However, HUD cannot be assured this will be the case with future obligation and expenditure deadlines.
- We appreciate HUD's agreement to add a description of its appeal process in future revisions of its plan.
- Comment 3** The procedures HUD described in its comments were not evidenced in its written plan provided for review and analysis during the audit; therefore, we did not revise the report. We appreciate HUD's agreement to add a description of its procedures for determining recapture amounts in future revisions of its plan.
- Comment 4** Government auditing standards define "significance" as the relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors. We assessed whether HUD's recapture and reallocation plan contained sufficient procedures to ensure that it met Recovery Act and other requirements and reported on deficiencies within the plan.
- We acknowledge that HUD staff had given thought to many aspects of the reallocation and recapture process; however, the written plan lacked specific details, which we concluded was a significant weakness. HUD should ensure that it has a documented plan for seamless continuity of its operations.